STATE OF NEW HAMPSHIRE
STATE LIQUOR COMMISSION

PERFORMANCE AUDIT REPORT
JULY 1994

TO THE FISCAL COMMITTEE OF THE GENERAL COURT:

We have conducted an audit of the New Hampshire State Liquor Commission (SLC) to address the recommendation made to you by the joint Legislative Performance Audit and Oversight Committee. This audit was conducted in accordance with generally accepted governmental auditing standards and accordingly included such procedures as we considered necessary in the circumstances.

The objectives of our audit were to analyze whether the current organizational structure supports efficient, effective, and economical management; assess current management practices and reporting relationships within the SLC; determine whether the management control structure is sufficient to ensure efficient operations and if the potential for waste, fraud and abuse is minimized; assess the operational efficiency and economy of the warehouse and transportation system; and determine if the marketing and merchandising operations efficiently and effectively fulfill the statutory responsibility to optimize the profitability of the SLC.

This report is the result of our evaluation of the information noted above and is intended solely to inform the Fiscal Committee of our findings and should not be used for any other purpose. This restriction is not intended to limit the distribution of this report, which upon acceptance by the Fiscal Committee is a matter of public record.

Office of Legislative Budget Assistant
OFFICE OF LEGISLATIVE BUDGET ASSISTANT

April 1995

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STATE OF NEW HAMPSHIRE
STATE LIQUOR COMMISSION

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ABBREVIATIONS

BATF	BUREAU OF ALCOHOL, TOBACCO, AND FIREARMS
CAFR	COMPREHENSIVE ANNUAL FINANCIAL REPORT
FAA	FEDERAL ALCOHOL ADMINISTRATION ACT
HRA	HUMAN RESOURCES ADMINISTRATOR
ISP	IN-STORE PROCESSOR
MIS	MANAGEMENT INFORMATION SYSTEMS
OITM	OFFICE OF INFORMATION TECHNOLOGY MANAGEMENT
PAU	PROGRAM APPROPRIATION UNIT
SLC	STATE LIQUOR COMMISSION

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STATE OF NEW HAMPSHIRE
STATE LIQUOR COMMISSION

SUMMARY

PURPOSE AND SCOPE OF AUDIT

This audit was performed at the request of the Fiscal Committee of the General Court consistent with recommendations from the joint Legislative Performance Audit and Oversight Committee and was conducted in accordance with generally accepted governmental auditing standards. It describes and analyzes the following: the State Liquor Commission's (SLC) organizational structure, its management practices and reporting relationships, the sufficiency of the management control structure to ensure efficient operations and minimize the potential for waste, fraud and abuse, the operational efficiency and economy of the warehouse and transportation system, and whether the marketing and merchandising operations efficiently and effectively fulfill the statutory responsibility to optimize the profitability of the SLC.

BACKGROUND

The New Hampshire State Liquor Commission was established by Chapter 99, NH Laws of 1933 (now codified as RSA 175-180, "Title XIII"). Three SLC commissioners are appointed by Governor and Council to serve staggered six-year terms. No more than two of the commissioners may be of the same political party. Governor and Council appoints one commissioner to a two-year term as chairman.

According to RSA 176:3 the primary duties of the Commission are: (1) optimizing profitability, (2) maintaining proper controls, (3) taking responsibility for effective and efficient operation, and (4) providing service to customers. Seven division directors report directly to the commissioners, as there is no level of management between commissioners and divisions. The SLC employs 305 full-time classified employees plus the three commissioners in its Concord headquarters, warehouse, and 68 stores.

Net profits from sales of alcoholic beverages were $40.4 million on sales of $208.7 million in FY 1994. We noted an upward trend (32.0 percent increase overall) in net profits for the six-year period from FY 1988 through FY 1993. However, the rate of increase took a downward turn in FY 1992. This downward trend continued through FY 1994. We also noted that income from fees, taxes, and other sources during the same time period increased from $13.9 million in FY 1988 to $16.5 million in FY 1994.

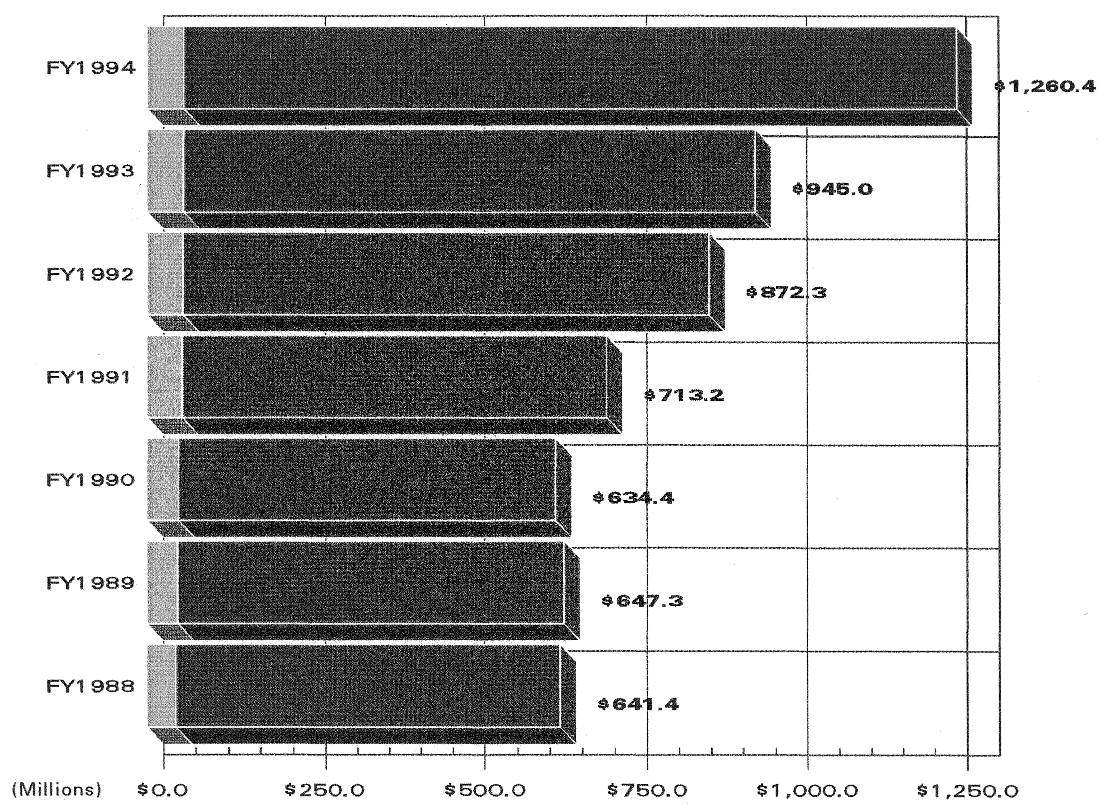
SUMMARY (Continued)

BACKGROUND (Continued)

Also moving downward is the SLC's proportional contribution to the State general fund. In FY 1988 the SLC contribution of over $45.1 million amounted to 7.0 percent of a general fund that had revenues of $641.4 million. By FY 1994 general fund revenue from all sources had increased 96.5 percent to $1.26 billion while the SLC transfer had increased only 26.1 percent to $56.9 million. This amounted to only 4.5 percent of general fund revenue (Figure 1).

FIGURE 1

SLC TRANSFERS AND GENERAL FUND REVENUES



	FY1994	FY1993	FY1992	FY1991	FY1990	FY1989	FY1988
All other General Fund	$1,203.5	$888.6	$816.6	$658.7	$585.3	$599.7	$596.3
SLC Transfers	$56.9	$56.4	$55.7	$54.5	$49.1	$47.6	$45.1

Source: LBA analysis of NH Comprehensive Financial Reports, FYs 1988-1994

SUMMARY (Continued)

BACKGROUND (Continued)

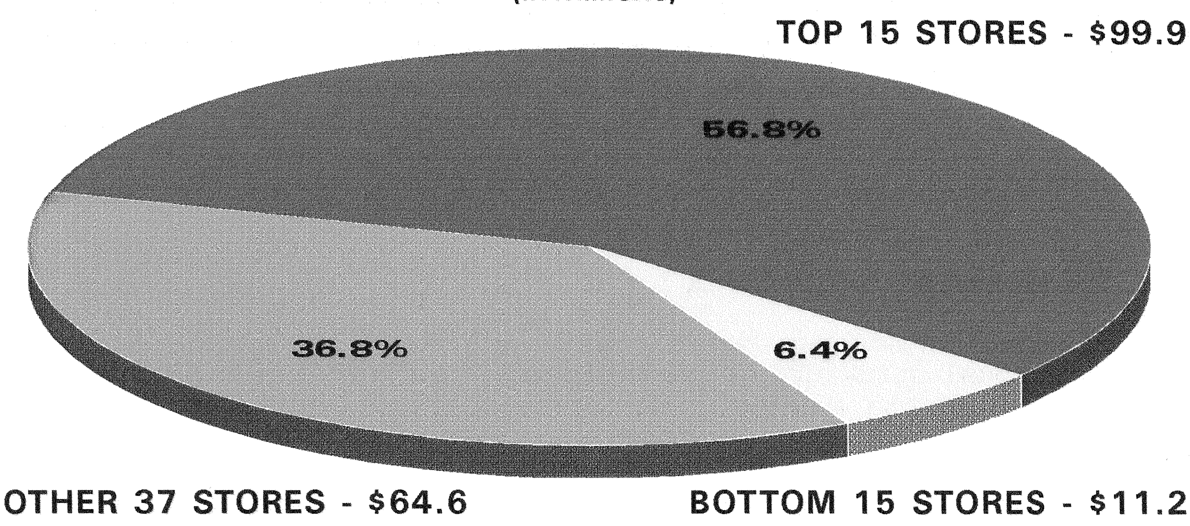
Detailed information on income by customer and product for FY 1992 through FY 1994 shows retail sales, primarily through the State's 68 wine and liquor outlet stores, decreased $1.4 million (minus nearly 1 percent), while sales to on-premise licensees (e.g., clubs, restaurants, and hotels) and off-premise licensees (e.g., supermarkets and convenience stores) increased $2 million and $4.9 million (8.8 percent and 20.3 percent) respectively. When viewed by product, wine sales increased $7.7 million (13 percent). During the period liquor sales decreased $2.2 million (minus 1.5 percent).

Sales from the SLC's top 15 stores amounted to $99.9 million, or 56.8 percent of store sales during FY 1993, when 67 stores were operating. At the other end of the sales spectrum, sales from the bottom 15 stores amounted to $11.2 million, or 6.4 percent of total store sales (Figure 2).

FIGURE 2

FY 1993 STORE SALES*

(in millions)



*FY 1993 $175.7 Million
Source: LBA analysis of SLC data

RESULTS IN BRIEF

The State Liquor Commission has always been a dependable source of money for State government. Over the six year period of our audit, FY 1988 to FY 1993, the SLC transferred over $308 million to the State's general fund. However, Americans have become more health and safety conscious and as a consequence are consuming less alcohol. In New Hampshire as elsewhere that behavior has translated into purchases of more wine and less liquor. The results have been felt at SLC cash registers and ultimately in the State's general fund.

While the SLC has responded admirably to its diminishing role in State government and the changing behavior of its customers by refurbishing many of its stores and putting forth a greater effort in marketing wine, it shows signs of being either unable or unwilling to adequately cope with its status as a State agency. This inability or unwillingness is manifested in observations documenting possible fraud and abuse as well as a cumbersome and inefficient organization without clear policies and procedures and without adequate planning and leadership.

PRINCIPAL FINDINGS AND RECOMMENDATIONS

We noted 46 observations and recommendations regarding the SLC. Seven of these address the agency's organizational structure, 13 concern management functions, and 26 deal with management controls.

Nine of the management control observations address possibly fraudulent actions concerning the SLC advertising contract, personnel actions, and State purchasing rules, as well as abuse in the form of unauthorized preferential treatment of a New Hampshire-based liquor manufacturer. These nine observations were forwarded to the attorney general for investigation. The complete text of the attorney general's response is found in Appendix E.

The SLC Should Be Reorganized

We observed numerous inadequacies and inefficiencies in the SLC organizational structure, beginning with the three-member Commission, but also including the sales-related divisions, administrative support, and enforcement functions. As a result of our observations, we recommend reorganizing the SLC as detailed in Chapter 2, pages 37-53. We believe the three-member SLC structure has outlived its usefulness and stands in the way of a more efficient, effective, and economical organization with streamlined and professional management. In addition, the organization of the marketing and sales structures we observed was inefficient and impeded the SLC's ability to further maximize sales revenue production. Finally, the organizational structure of the SLC's administrative units did not provide optimum support and functioning. The current structure is cumbersome, contains unusual reporting relationships and systemic operational inefficiencies.

SUMMARY (Continued)

PRINCIPAL FINDINGS AND RECOMMENDATIONS (Continued)

Management Functions Need Improving

Problems with the SLC's fractionalized organizational structure translate into management problems in key functions. Areas of concern include planning in the marketing and sales function, warehouse safety, MIS planning and support, human resources including staff training, and others as detailed in Chapter 3, pages 55-79. These problems serve to weaken SLC operations, negatively impact efficiency and effectiveness, and diminish the SLC's ability to optimize profits and contribute to State revenues.

Management Controls Do Not Provide Sufficient Assurances Against Waste, Fraud, And Abuse

We determined the SLC's management control structure needed improvements to ensure efficient operations and minimize the potential for fraud and abuse. As previously noted, we reviewed possibly fraudulent actions concerning the advertising contract, personnel actions, and State purchasing rules, as well as abuse in the form of unauthorized preferential treatment of a New Hampshire-based liquor manufacturer as detailed in Chapter 4, pages 82-92. In the remaining sections of Chapter 4, pages 93-121, we observed additional management control problems. These included numerous problems within the administrative support functions concerning accounting and MIS. Also, store operations should update its policies and procedures and review security procedures in retail locations, while warehouse operations need additional controls for inventory and security. Improvements in file security and documentation of significant processes are needed in enforcement and regulation. Additional administrative rules should be promulgated regarding the bailment warehouse, assessing fines and suspending licenses, and authority to make special exceptions to SLC rules. Finally, some advertising practices may be out of compliance with State and federal laws.

AGENCY COMMENTS

In commenting on this report, the SLC concurred with 12 of our observations and recommendations, concurred in part with 25, and did not concur with nine. The complete text of the agency's responses is found in Appendix D.

We reviewed the SLC's responses and found no reason to make substantive changes to our observations and recommendations. We have also taken the unusual step of providing rebuttals to many of the SLC's responses. These rebuttals follow the agency's responses in Appendix D.

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SUMMARY OF ACCOMPLISHMENTS

The New Hampshire State Liquor Commission celebrates its 60th birthday this year. During these 60 years, our continuing mission has remained very positive. Our successes were achieved through a quality of leadership that understood the fundamental underlying foundation of our reason for being and a willingness to build and grow on this foundation.

The strength of this foundation is sound and solid. The original identified purpose was to provide a rich source of state revenue, to maintain a strict form of social control over the traffic of a commodity that is inherently susceptible to abuse, and to give purchasers assurance that the goods they purchase are legal, tax-paid, pure in quality and exactly as represented in every particular, and at a reasonable price. This purpose still stands firmly today.

Through the years the Commission's successes were many, and New Hampshire was recognized as the leader in progress resulting from many pioneering firsts. This overall success came from a willingness to explore, to broaden our scope of vision, to continually move forward and simply to take the appropriate actions necessary to achieve and maximize the goals established within our foundation's purpose.

This Commission, during the seven years generally focused on during this audit, continued these efforts towards achieving those firmly established goals and stands proud in recognizing the beneficial results accruing to the citizens of our State.

Our efforts centered on a firm dedication towards our mission while constantly keeping faith with our promise of fairness, openness and consistency, yet still maintaining the flexibility necessary toward meeting our public challenge.

The problems within the industry began to come to light in the early nineties. The national market was now considered a mature market. Further impacting was the downward trend in national sales due to people becoming more cognizant and responsive to the health and social abuses resulting from the irresponsible use of alcohol. It is very important to note that consumption nationwide diminished well over 20% from the previous decade. New Hampshire had a further problem with the Canadian/American monetary exchange rate approaching 40% and turning away a significant segment of our market. The economy in general faced a major downturn impacting on our sales.

TDD Access: Relay NH 1-800-735-2964

The State Liquor Commission, in the traditional New Hampshire custom, faced these problems head on, taking numerous actions designed to offset these problems and the national trend. The resultant success had been admirable to the point where industry as a whole recognizes New Hampshire and the State Liquor Commission as being amongst the best merchandisers and retailers in the country. Officials from other states such as Virginia, West Virginia, Idaho and others like the country of Finland have come to New Hampshire to see why and how we are accomplishing our excellent results, and they are attempting to emulate our operation and style.

In order to continue meeting our charge of providing a rich source of state revenue, our actions focused primarily on two fronts, i.e. Economic and Marketing.

Economic Fronts:

- The New Hampshire State Liquor Commission's operating performance is outstanding as evidenced by the following comparison of its operating ratios to industry averages as a nationally recognized leader in the retail market.

	INDUSTRY (1) AVERAGE	(2) WAL-MART	1994 (3) NHSLC
G.P. as a % of Sales	22.70%	21.50%	28.62%
Operating Exp. as a % of Sales	21.70%	15.10%	8.69%
Pre-tax Profit as a % of Sales	1.00%	6.40%	20.52%
Inventory Turns	7.30	6.20	11.45
Sales to Total Assets	3.70	2.70	7.92
Sales per Sq. Ft.	N/A	$279.00	$534.46

(1) Source: 1993 Robert Morris & Associates
(2) Source: 1992 Wal-Mart Annual Report
(3) Source: 1994 CAFR (Calculations include liquor, sweeps & bailment revenues; expenses are net of enforcement expenses.)

- During Fiscal Years 91 through 94, Commission reduced the permanent personnel complement over 25%.

- Closed six retail stores which were deemed unnecessary or marginally profitable. In addition, several others were downsized and/or relocated in order to reduce costs (by almost $35,000) while optimizing sales. More than half of our stores were refurbished and/or rehabilitated.

- Converted our State Liquor Commission Warehouse to a bailment operation resulting in $3,375,000 dollars of new gross revenue in less than 3 1/2 years. Additionally, it relieved the State General Fund of six to nine million dollars in cash flow requirements.

- Introduced the state of the art point of sale cash register system at every location, finally giving the Commission the ability to collect and analyze data both at the unit level and in the aggregate necessary to make meaningful decisions.

- Introduced inventory control and a quick response "feeder system" to outlying retail stores.

- Initiated a fine system for licensee violations in March of 1990 which has since realized new revenues of $359,030 through 1994 for the General Fund.

Marketing Front:

- Introduced the "Top 25" program, which is a pricing and merchandising strategy that encourages cross-border sales in a very competitive market place.

- Increased our premium wine outlets from 3 in 1989 to over 21 in 1994. This is an effort to confront a mature market by developing the wine market in New Hampshire heretofore treated as secondary. Results include better convenience for licensees and the general public and an increase in retail wine sales by 36 % since 1990 through Fiscal Year 1994.

- Initiated a "Wine & Food" program both on television and on exhibition in various parts of the State.

- Began programs designed towards micro-targeting sales efforts towards special consumer groups.

- Initiated the development of a shelf management program designed to emphasize products that will produce an increase in incremental sales and maximize retail gross profit.

Some overall results:

- Gross sales during the 7-year audit period grew 21.6% from $171.6 million to $208.7 million.

- During Fiscal Years 1987 through 1994 sales in the aggregate totalled $1.35 billion, with a total gross revenue contribution of approximately 1/2 billion dollars. The net effect is that the State Liquor Commission, during its 60 years of existence has returned $1.13 billion in net revenue to the General Fund and, remarkably, 25% or almost $300 million, came from this 7-year period.

- According to DISCUS (The Distilled Spirits Council of the United States), in its 1992 Report on Public Revenues from Alcoholic Beverages, control states and license states generated per capita revenue of $37.57 and $36.58, respectively. NHSLC lead all control states in per capita revenue at $75.08; over twice the national average of all states.

- While NHSLC was #1 in per capita revenue among control states, it had the lowest expenses as a percent of sales of any control state with retail operations; expenses as a percent of sales were 5% less than the next closest control state with retail operations.

- One of the factors involved in NHSLC's success has been its ability to control operating expenses. Over the past 5 years, the NHSLC has been able to operate at approximately the same funding level in spite of labor and occupancy cost increases.

- Operating expense as a percent of net sales shrank from 10.0% in 1988 to 9.3% in 1994. This saved the state $1.5 million in 1994.

This brief presentation which attempts to highlight some of the economic benefits to our citizens is unfortunately quiet in the social control benefits accruing to our citizens, but those are meaningful and many.

Suffice it to say that the State Liquor Commission's contribution to the citizens of this State is a great one. This contribution has successfully given the Legislature significant dollars needed to fund worthy programs that would otherwise not be available for our citizens without a major increase in taxes. The State Liquor Commission system has worked and has worked well. There is assuredly always room for improvement, and the State Liquor Commission has continually attempted to improve its overall operation and will continue to do so. The Legislature should exercise a great deal of caution and undertake a truly impartial study prior to making any drastic changes that may impact negatively on this proven system.

STATE OF NEW HAMPSHIRE
STATE LIQUOR COMMISSION

LBA RECOMMENDATION SUMMARY

OBS. NO.	PAGE	REQUIRES LEGISLATIVE ACTION YES/NO	RECOMMENDATION	AGENCY RESPONSE
1	40	YES	Reorganize the SLC under the executive direction of a single commissioner. Establish a part-time board to hear administrative appeals.	Do Not Concur
2	41	YES	Reorganize the SLC's four sales-related divisions (marketing and merchandising, purchasing, warehouse, and store operations) into one sales and marketing division.	Concur In Part
3	43	YES	Reorganize the SLC's three administrative-related units (financial management, MIS, and human resources administration) into one administrative services division.	Concur In Part
4	45	NO	Replace the supervisor/manager system and reclassify six positions as district supervisors.	Concur In Part
5	48	NO	Field assistant chiefs should not carry licensee caseloads.	Concur In Part
6	49	NO	Reclassify the administrative assistant chief position.	Do Not Concur

LBA RECOMMENDATION SUMMARY (Continued)

OBS. NO.	PAGE	REQUIRES LEGISLATIVE ACTION YES/NO	RECOMMENDATION	AGENCY RESPONSE
7	52	NO	Abolish the senior liquor investigator classification.	Do Not Concur
8	55	NO	Improve the marketing planning process.	Concur In Part
9	57	NO	Review the advertising budget.	Concur In Part
10	58	NO	Review store staffing levels.	Concur
11	60	YES	Assess costs and benefits of centralizing warehouse operations and report to the Legislature by the 1996 session. Request authority to competitively bid the State's only liquor, wine, and beverage warehouse license.	Concur In Part
12	62	NO	Develop and implement a safety program for the warehouse.	Concur In Part
13	64	NO	Acquire software to support research in the marketing and sales function.	Concur In Part
14	66	NO	Ensure timely notification to stores of upcoming sales and promotions. Continue to develop or purchase an electronic mail system. Develop effective reports and analytical programs.	Concur In Part

LBA RECOMMENDATION SUMMARY (Continued)

OBS. NO.	PAGE	REQUIRES LEGISLATIVE ACTION YES/NO	RECOMMENDATION	AGENCY RESPONSE
15	68	NO	Make needed improvements to the accounting system.	Concur
16	69	YES	Evaluate training needs and implement training programs in all divisions. Establish a training coordinator position.	Concur In Part
17	74	NO	Ensure all full-time classified employees receive written performance evaluations annually.	Concur
18	75	NO	Follow procedures required by the Division of Personnel administrative rules for transfer or reassignment.	Concur In Part
19	78	YES	Analyze the effectiveness of a two-year renewal cycle for most liquor licenses.	Concur
20	79	NO	Provide in-home office telephone lines and telephone answering machines for investigators.	Concur In Part
21	82	NO	Attorney general investigate whether SLC commissioners used contract funds for reasons other than appropriated. *	Do Not Concur
22	83	NO	Attorney general investigate whether SLC commissioners inappropriately awarded a no-bid contract to the MIS director. *	Do Not Concur

* For attorney general response, see Appendix E.

LBA RECOMMENDATION SUMMARY (Continued)

OBS. NO.	PAGE	REQUIRES LEGISLATIVE ACTION YES/NO	RECOMMENDATION	AGENCY RESPONSE
23	84	NO	Attorney general investigate whether SLC commissioners or the MIS director violated conflict of interest statute. *	Do Not Concur
24	85	NO	Attorney general investigate to clarify ownership and other rights to the shelf management program. *	Concur
25	86	NO	Attorney general investigate whether awarding subcontract to the SLC's MIS director violated terms and conditions of the advertising contract. *	Do Not Concur
26	87	NO	Attorney general investigate whether the SLC violated State purchasing requirements. *	Concur
27	88	NO	Attorney general investigate whether SLC commissioners violated State law regarding temporary and part-time employees. SLC seek reimbursement for health and dental insurance premiums wrongfully paid. *	Concur In Part
28	90	NO	Attorney general investigate whether SLC commissioners used official authority or influence to secure an appointment to the State classified service. *	Concur In Part

* For attorney general response, see Appendix E.

LBA RECOMMENDATION SUMMARY (Continued)

OBS. NO.	PAGE	REQUIRES LEGISLATIVE ACTION YES/NO	RECOMMENDATION	AGENCY RESPONSE
29	91	NO	Attorney general investigate whether the SLC violated State or federal laws pertaining to treatment of manufacturers of alcoholic beverages. SLC require New Hampshire-based manufacturers to pay bailment and other warehouse charges incurred from March 1992 to present. *	Concur In Part
30	93	NO	Reevaluate policies and procedures in store operations. Revise store manual.	Concur In Part
31	95	NO	Develop and implement written policies and procedures governing store management deposit withholding activity.	Concur
32	96	NO	Conduct thorough security audit of State stores.	Concur
33	97	NO	Improve Concord warehouse security.	Concur In Part
34	98	NO	Improve supervisory review of warehouse activity.	Concur In Part
35	100	NO	Develop and implement written, comprehensive operating policies and procedures for financial management.	Concur In Part

* For attorney general response, see Appendix E.

LBA RECOMMENDATION SUMMARY (Continued)

OBS. NO.	PAGE	REQUIRES LEGISLATIVE ACTION YES/NO	RECOMMENDATION	AGENCY RESPONSE
36	103	NO	Ensure that all financial management unit supervisors conduct adequate supervisory review. Chief accountant should supervise work of unit supervisors.	Concur In Part
37	104	NO	Develop written internal policies and procedures regarding purpose and use of the petty cash and change fund.	Concur
38	107	NO	Develop, implement, and enforce policies and procedures regarding cash and checks received by financial management general ledger unit.	Concur In Part
39	108	NO	Ensure the X-Y plotter is placed on the SLC's fixed asset inventory.	Concur
40	109	NO	Work with Office of Information Technology Management to develop an information technology plan.	Concur
41	111	NO	Supervisors should reconcile load receiving summaries and packing slips when visiting stores every two weeks.	Concur In Part
42	113	NO	Clear paid fines. Complete software modifications necessary to enter fine payment information into the accounting system. Develop and implement policies and procedures.	Concur

LBA RECOMMENDATION SUMMARY (Continued)

OBS. NO.	PAGE	REQUIRES LEGISLATIVE ACTION YES/NO	RECOMMENDATION	AGENCY RESPONSE
43	115	NO	Repair or replace the Enforcement and Regulation Division licensee records file cabinet with a locking cabinet. Develop procedures regarding file security and access.	Concur in Part
44	117	NO	Promulgate administrative rules and procedures regarding: (1) the bailment warehouse, (2) administrative fines, and (3) specify when exceptions to rules may be granted.	Concur in Part
45	119	NO	Seek a waiver from Bureau of Alcohol, Tobacco, and Firearms regarding cooperative advertising.	Do Not Concur
46	120	YES	Request clarification of statutory intent regarding RSA 175:4, advertising.	Do Not Concur

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STATE OF NEW HAMPSHIRE
LIQUOR COMMISSION

SUMMARY OF AGENCY RESPONSE & ACTION

OBS NO.	PAGE	LBA RECOMMENDATION		AGENCY RESPONSE RECOMMENDATION TO AUDIT	AGENCY ACTION
1	40 & D-1	Single Commissioner		Contrary to the observation, the Commission has demonstrated great success under a proven system.	Concerted effort to correct shortcomings & continue to improve total operation.
2	41 & D-5	Reorganize Sales & Marketing Functions		One modern organizational setup is a matrix which clearly resembles the Commission's operation.	Continue efforts to coordinate all activities to improve an already efficient & profitable operation.
3	43 & D-7	Reorganize Administrative Functions		Contrary to observation, profitability is already being optimized. New layer of management not required.	Commission has developed better teamwork & will continue to improve efforts to coordinate.
4	45 & D-10	Abolish Supervisor/ Manager System		This creates a new layer of management which is not essential but preferable.	We will explore feasibility & seek funding to implement.
5	48 & D-14	Relieve Asst. Chiefs of Caseloads		Creates a new layer of management. We do not believe there is a breakdown in supervision placing the State at risk.	Filling 2 previous vacancies has relieved the cited burden significantly. We will attempt to reinstate cut positions in future.
6	49 & D-16	Administrative Assistant Chief Position is Unnecessary		LBA recommends a return to a system that did not work as well as the current system.	No action warranted.
7	52 & D-21	Abolish Senior Liquor Investigator Classification		The Commission does not believe a single job specification can perform all the varied duties required.	We will review job requirements & submit any necessary changes to the Division of Personnel to review.
8	55 & D-26	Improve Market Planning Process		Several personnel changes resulted in an inability to maintain consistent planning documentation.	Positions are currently filled & a Business Plan developed last August by all Directors for future marketing & operating activities.
9	57 & D-29	Advertising Budget Should be Reviewed		SLC relies on media experts as to how to reach & influence the buying public.	SLC will continue cost-benefit analysis & insist on bottom line benefits to the Agency's mission.

STATE OF NEW HAMPSHIRE
LIQUOR COMMISSION

SUMMARY OF AGENCY RESPONSE & ACTION (Continued)

OBS NO.	PAGE	LBA RECOMMENDATION		AGENCY RESPONSE RECOMMENDATION TO AUDIT	AGENCY ACTION
10	58 & D-33	Store Staffing Levels Should Be Reviewed		SLC concurs but recognized the need for post budget restraints.	Commission will continue to review staffing levels & take appropriate budget action when necessary. We have reduced our permanent staffing by 25% during audit period.
11	60 & D-34	Assess Cost/Benefit of a One Warehouse Operation		SLC has continually recommended a single warehouse operation.	In lieu of a single warehouse, Commission will place privately owned warehouse out to bid by end of May.
12	62 & D-36	Safety Factors Account For Majority of W/C Claims in SLC Warehouse		The SLC has utilized prevention & claims management resources as available.	SLC, in conjunction with Risk Management, will further develop & implement a formal safety program during this calendar year.
13	64 & D-38	Improve Analytical Capabilities For Marketing & Sales		Commission does have in place analytical data & sales reports to target performance	SLC currently installing upgraded hardware & new software which will enhance necessary forecasting & research requirement.
14	66 & D-40	MIS Support for Stores Should Be Improved		SLC concurs & is in process of developing electronic mail to all outlets.	Improve communications with stores while developing a user friendly program to identify & correct warehouse stock-outs.
15	68 & D-42	Accounting Software Needs Upgrading		SLC concurs.	Currently in process of implementing new software package to be completed by July 1.
16	69 & D-43	In-Service Training Improvements Needed		SLC has made training a priority. Funding cuts have hampered the suggested method.	Lowest cost training programs are already developed & underway that will improve employee knowledge.
17	74 & D-51	SLC Employees Not Evaluated Annually As Required		SLC concurs.	All employees will be evaluated as required on an annual basis.
18	75 & D-52	Employees Working Outside Of Own Division Without Division of Personnel Approval		SLC special assignments were job related & temporary in nature.	Where required we have submitted supplemental job descriptions to Division of Personnel.

SUMMARY OF AGENCY RESPONSE & ACTION (Continued)

OBS NO.	PAGE	LBA RECOMMENDATION		AGENCY RESPONSE RECOMENDATION TO AUDIT	AGENCY ACTION
19	78 & D-54	Analyze the Effectiveness Of a 2-Year License Renewal Cycle		SLC concurs.	Even during audit SLC was investigating the feasibility. We expect to implement within 1 year.
20	79 & D-56	Material Support for Home Offices of Liquor Investigators Should Be Increased		SLC concurs in part.	SLC has taken action providing the required material support for home offices of investigators.
21	82 & D-58	Advertising Contract Used For Non-Advertising Purposes		SLC has traditionally understood advertising to include merchandising which adds incremental sales.	Have advised the Legislature & Administrative Services of the clarified definition of advertising for FY 96 and 97 budget.
22	83 & D-61	No-Bid Contract Inappropriately Awarded to MIS Director		SLC consulted with the appropriate agency & was advised that the arrangement was proper. The savings were significant.	All present & future procurement will be accomplished using normal state procedures.
23	84 & D-61	Conflict of Interest for MIS Director in Accepting Shelf Management Contract		Same as 22.	
24	85 & D-65	Ownership of Intellectual Property in Question		SLC concurs. State should have ownership.	MIS director has signed over all ownership rights to the State.
25	86 & D-61	Breach of Advertising Contract Terms & Conditions		Same as 22.	
26	87 & D-67	Noncompliance With State Purchasing Requirements		SLC was advised by Chief Accountant that these were replacement items & as such required only quotes.	Purchasing policy in place during 1994 to require several sign-offs on all purchased goods or services.
27	88 & D-68	Noncompliance With State Laws Regarding Temporary & Part-time Employees		Commission was advised & believed approvals were required only after 1 year of temporary employment beyond 30 hours.	Policy in place prohibiting any extended temporary hours beyond 30.
28	90 & D-68	Abuse of State Laws Regarding Appointments to Classified State Service by SLC Commissioners		Same as 27. Additionally, had a position been approved the Commission would have posted it as required making it available for all.	Same as 27. New positions will continue to be developed through Dept. of Personnel & posted.

SUMMARY OF AGENCY RESPONSE & ACTION (Continued)

OBS NO.	PAGE	LBA RECOMMENDATION		AGENCY RESPONSE RECOMENDATION TO AUDIT	AGENCY ACTION
29	91 & D-71	Preferential Treatment of Local Liquor Manufacturer		State liquor manufacturer license incorporates their own warehouse ability. SLC did not deem it fair to charge a dual expense of bailment.	Commission will develop & adopt a written policy concerning bailment charges & apply equally to all manufacturers.
30	93 & D-72	Insufficient Compliance With Store Operations Manual		SLC concurs in part with observation due to personnel vacancies & shortages.	Store operations manual is in process of being updated to comply with current & improved store practices.
31	95 & D-74	Policies & Procedures Needed For Deposit Withholdings		SLC concurs with observation & previous attempts to correct were prevented by Administrative Services.	Commission will submit another request to increase change fund to Governor & Council.
32	96 & D-75	Security of Store Stores May Be Insufficient		Commission concurs despite low shrink rate.	Security measures continue to be reviewed & improvements to all stores'security will be developed as funding permits.
33	97 & D-77	Insufficient Security for Concord Warehouse		Warehouse security has been made a priority as actions taken demonstrate.	Money has been requested in budget to further address other security measures deemed necessary
34	98 & D-79	Insufficient Supervisory Review in Concord Warehouse		The SLC believes there is reasonable supervisory review as our average inventory shrink rate is .044% as compared to the retail industry average of 1.9%.	Supervisory review will be enhanced to incorporate the recommended action deemed feasible & appropriate.
35	100 & D-83	Financial Management Policies & Procedures Insufficiently Documented		The Commission concurs in part, although many developed procedures exist, but not in writing.	The SLC will continue developing written policies & combine them into a comprehensive operating manual.
36	103 & D-84	Insufficient Supervisory Review In Financial Management Division		The SLC believes it does adequate supervisory review in Financial Management hampered only when vacancies occur.	The new accounting system software will allow more flexibility in posting & reconciliation. Further review will be undertaken for improvements that are cost effective.

SUMMARY OF AGENCY RESPONSE & ACTION (Continued)

OBS NO.	PAGE	LBA RECOMMENDATION		AGENCY RESPONSE RECOMENDATION TO AUDIT	AGENCY ACTION
37	104 & D-88	Inappropriate Use of Petty Cash & Change Fund		The Commission concurs with the observation & recommendation.	Written policies & procedures will be incorporated into the comprehensive operating manual currently under development.
38	107 & D-89	Insufficient Security For Cash & Checks		SLC concurs in part. We do have a restrictive endorsement policy & have reinforced its use by personnel.	Work practices will be improved by policies in the operating manual & safe combinations changed & restricted to supervisory personnel only.
39	108 & D-93	Disposition of Printer Purchased Through Shelf Management Contract Is Questionable		Commission concurs.	The X-Y-Z Plotter is now included in the fixed asset inventory as SLC property.
40	109 & D-94	Insufficient MIS Policies & Oversight		The SLC concurs that paper documentation is minimal but that most computer policies & procedures are in the computer itself.	Written policy documentation will be improved including further development of consistent standards & testing criteria.
41	111 & D-96	Insufficient Supervision Of Inventory Tracking Procedures		The Commission's records show a loss/gain amount of $599,336 over the 7-year period.	The Commission will develop procedures necessary to enhance supervisory review as may be economically feasible.
42	113 & D-98	Inadequate Procedures For Processing License Fees & Fines		SLC concurs.	SLC has since developed at least a 1st draft of a personnel instruction manual to be completed. All checks are now being stamped immediately upon receipt by individual reviewing them.
43	115 & D-99	Enforcement Licensee Records Are Neither Secure Nor Complete		We concur in part.	Office security has been corrected by building a wall & putting on a security gate.
44	117 & D-102	Additional Administrative Rules Should be Promulgated For Fines, Bailment & Wine Tastings		Rules have not been developed because the SLC has written policies & procedures for user vendors & suppliers.	The Commission will develop & submit rules during calendar year 95.

STATE OF NEW HAMPSHIRE
LIQUOR COMMISSION

SUMMARY OF AGENCY RESPONSE & ACTION (Continued)

OBS NO.	PAGE	LBA RECOMMENDATION		AGENCY RESPONSE RECOMENDATION TO AUDIT	AGENCY ACTION
45	119 & D-106	Cooperative Advertising.		The Commission does not participate in what is considered cooperative advertising.	Should the BATF develop rules affecting this situation, the Commission shall cease its portion of the advertisement.
46	120 & D-108	Clarification of Intent Of RSA 175:4, Relative to In-State Advertising		The SLC does not agree with the observation & continues to believe the 80-20 split in out of state/in state advertising refers to budgeted advertising dollars.	The SLC will attempt to clarify through legislation the understanding of the 80/20 split.

STATE OF NEW HAMPSHIRE
STATE LIQUOR COMMISSION

INTRODUCTION

1. INTRODUCTION

1.1 OVERVIEW

After national prohibition ended with passage of the 21st Amendment to the U.S. Constitution in 1933, responsibility for regulating consumption, manufacture, and transportation of liquor was delegated to state governments. Each state adopted its own system of alcohol control and regulation within its own boundaries. Fifty regulatory systems with differing laws and regulations resulted.

The New Hampshire State Liquor Commission (SLC) was established by Chapter 99, NH Laws of 1933 (now codified as RSA 175-180, "Title XIII"). Title XIII delineates the powers and administrative functions of the SLC as well as store operations, licensing, enforcement, and beverage distributor agreements. Title XIII was recodified in 1990.

New Hampshire is one of 18 "control states." Although variances among these states are common, control states generally regulate alcohol through a government agency directly involved in wholesale distribution and in most cases retail merchandising of alcohol products. In ten control states, including New Hampshire, the same state agency also licenses private sellers of alcohol and enforces state alcohol laws, while in five other states the agencies have licensing but not enforcement responsibilities. In three control states the agencies have neither licensing nor enforcement responsibilities. Other control states in New England include Maine and Vermont (Appendix A). The 32 states which only license persons engaged in alcohol distribution and sales are called "license states."

Funding

The Legislature approves a budget each biennium for the SLC. For FY 1994 the agency's operating expenses were $19.4 million. Clearing accounts are used to pay for the SLC's purchases of liquor and wine stock and for transportation of products from the warehouse to State stores. In FY 1994 liquor and wine purchases by the SLC amounted to almost $148.1 million, while transportation expenditures were $828,200. Funds used for these purposes are advanced to the SLC from the general fund.

All gross revenues from sales, as well as revenues derived from wholesale distributors and beverage manufacturer's fees (generally referred to as the beer tax) license fees, fines, and the bailment warehouse, are deposited daily into the State general fund with one exception. RSA 177:8(II) requires revenues from special markups on commemorative bottles of historical significance to be credited to the historical fund.

1. INTRODUCTION (Continued)

1.1 OVERVIEW (Continued)

Results of Operations

Through review of the State's Comprehensive Annual Financial Report (CAFR) for FYs 1988-1994, we identified the SLC's two primary revenue streams: (1) liquor and wine sales and (2) non-operating revenues including beer taxes, licensee fees, and miscellaneous items (Table 1).

Net profits from sales of alcoholic beverages were $40.4 million on sales of $208.7 million in FY 1994. We noted an upward trend (32.0 percent increase overall) in net profits for the six-year period from FY 1988 through FY 1993. However, the rate of increase took a downward turn in FY 1992. This downward trend continued through FY 1994. We also noted that income from fees, taxes, and other sources during the same time period increased from $13.9 million in FY 1988 to $16.5 million in FY 1994.

Income from liquor and wine sales represents the largest source of income for the SLC. The $40.4 million in FY 1994 from liquor and wine sales comprised 71.0 percent of the $56.9 million in net revenues transferred from the agency to the general fund. Beer taxes were the second largest income source, comprising $11 million (19.3 percent) in revenues transferred. License fees represented $2.8 million (4.9 percent), while miscellaneous items contributed $2.7 million (4.8 percent).

Detailed information on income by customer and product was only available for three years, FY 1992 through FY 1994. That information showed retail sales, primarily through the State's 68 wine and liquor outlet stores, decreased $1.4 million (minus nearly 1 percent), while sales to on-premise licensees (e.g., clubs, restaurants, and hotels) and off-premise licensees (e.g., supermarkets and convenience stores) increased $2 million and $4.9 million (8.8 percent and 20.3 percent) respectively. When viewed by product, wine sales increased $7.7 million (13 percent). During the period liquor sales decreased $2.2 million (minus 1.5 percent) (Table 2).

We analyzed information provided by the SLC to determine which of the 68 State liquor and wine outlet stores sold the most alcoholic beverages in the State from FYs 1988-1993. Primarily the same State liquor stores ranked as the top five sellers from year to year. These top five State stores, ranked from highest to lowest, were: (1) Portsmouth (#38), (2) Hampton (#73), (3) Salem (#34), (4) Hooksett North (#66), and (5) Nashua (#50). All of these stores except Nashua were in the top five every year. In both FY 1993 and FY 1992 Nashua (#50) ranked seventh among all stores, while another Nashua store (#69) ranked fifth.

TABLE 1

STATE OF NEW HAMPSHIRE
LIQUOR COMMISSION

STATEMENT OF REVENUES AND EXPENSES

	1994	1993	1992	1991	1990	1989	1988	TOTAL FY 94 to 88
SALE OF WINE AND LIQUOR	$208,659,062	$208,578,882	$204,651,105	$194,283,353	$186,754,283	$178,728,237	$171,570,179	$1,353,225,101
COST OF WINE AND LIQUOR	148,936,720	147,936,380	144,948,755	137,353,951	133,612,334	128,518,201	123,180,072	964,486,413
GROSS PROFIT	$ 59,722,342	$ 60,642,502	$ 59,702,350	$ 56,929,402	$ 53,141,949	$ 50,210,036	$ 48,390,107	$ 388,738,688
OPERATING EXPENSES								
Personnel Services	$ 13,838,973	$ 13,724,289	$ 13,466,057	$ 13,680,474	$ 13,858,160	$ 12,890,948	$ 12,001,221	$ 93,460,122
Current Expenses	5,517,449	5,669,707	5,832,305	5,886,310	5,344,352	5,402,067	5,145,796	38,797,986
Total Operating Expenses	19,356,422	19,393,996	19,298,362	19,566,784	19,202,512	18,293,015	17,147,017	132,258,108
NET PROFIT[1]	$ 40,365,920	$ 41,248,506	$ 40,403,988	$ 37,362,618	$ 33,939,437	$ 31,917,021	$ 31,243,090	$ 256,480,580
NON-OPERATING REVENUES								
Licenses	$ 2,818,229	$ 2,775,553	$ 2,752,335	$ 2,658,694	$ 2,065,660	$ 1,874,635	$ 2,069,546	$ 17,014,652
Beer Taxes	11,000,428	10,984,381	11,180,797	12,794,251	11,525,847	11,526,642	11,382,687	80,395,033
Other	2,704,982	1,362,327	1,366,034	1,652,476	1,576,193	2,316,535	415,434	11,393,981
Total Non-operating Revenue	16,523,639	15,122,261	15,299,166	17,105,421	15,167,700	15,717,812	13,867,667	108,803,666
TRANSFER TO GENERAL FUND[2]	$ 56,889,559	$ 56,370,767	$ 55,703,154	$ 54,468,039	$ 49,107,137	$ 47,634,833	$ 45,110,757	$ 365,284,246

NOTES:

[1] Net Profit = gross profit minus total operating expenses

[2] Transfer to general fund = net profit plus total non-operating revenue

SOURCE: Comprehensive Annual Financial Report (CAFR) various years.

1. INTRODUCTION (Continued)

1.1 OVERVIEW (Continued)

<u>TABLE 2</u>

STATE OF NEW HAMPSHIRE
LIQUOR COMMISSION
SALES BY CUSTOMER AND PRODUCT

(figures in millions)

BY CUSTOMER	1994	1993	1992
RETAIL	$156.5	$157.5	$157.9
ON-PREMISE*	24.6	23.7	22.6
OFF-PREMISE*	29.0	27.2	24.1
TOTAL	$210.1	$208.4	$204.6

BY PRODUCT	1994	1993	1992
WINE	$ 66.9	$ 63.5	$ 59.2
SPIRITS	143.2	144.9	145.4
TOTAL	$210.1	$208.4	$204.6

Source: LBA analysis from SLC data
*NOTE: Includes sales through stores and warehouses.
The total sales figures for 1993 and 1994 reported in Table 2 differ from Table 1 because Table 2 uses unaudited data.

Although income from liquor and wine sales has continued to increase in the State, evidence from the liquor industry indicates a trend towards decreased consumption of alcoholic beverages nationwide. The continued strength of the SLC's operations lies in the State's geography, the legislative mandate to attract out-of-state consumers, and in the infrastructure that has evolved over the years which features conveniently located stores along major interstate highways and the Massachusetts border. New Hampshire's geography has made it desirable as both a tourist destination and a second home to people from other states. Support for the role of these factors as contributors to the success of the State's liquor sales monopoly is evidenced in the locations of the top 15 stores, which include those along the Massachusetts and Vermont borders, the interstate highways, and the tourist areas of Conway and Gorham (Figure 3). For example, in FY 1993 when there were 67 stores, sales from the top 15 stores amounted to $99.9 million, or about 56.8 percent of store sales. At the other end of the sales spectrum, sales from the bottom 15 stores amounted to $11.2 million,

1. INTRODUCTION (Continued)

1.1 OVERVIEW (Continued)

or 6.4 percent of total store sales (Appendix B). A more recent factor supporting strong sales performance is the SLC's emphasis on wine marketing, which is discussed further in the significant achievements section at the end of this chapter.

1.2 ORGANIZATIONAL STRUCTURE

RSA 176 establishes the three-member Liquor Commission and specifies its duties and requirements, as well as those of the internal divisions. The three commissioners are appointed by Governor and Council to serve staggered six-year terms. No more than two of the commissioners may be of the same political party. Governor and Council appoints one commissioner to a two-year term as chairman.

According to RSA 176:3 the primary duties of the Commission are: (1) optimizing profitability, (2) maintaining proper controls, (3) effective and efficient operation, and (4) providing service to customers. The seven internal divisions report directly to the commissioners, as there is no middle level of management between commissioners and divisions. In all but one case, the divisions have directors responsible for managing ongoing operations.

The warehouse and transportation director position has been vacant for several years. SLC personnel reported the position was not filled as a cost saving measure after the former director left. The warehouse and transportation superintendent supervises the day-to-day operations of the warehouse and transportation functions. However, this position reports to the financial management director on a monthly basis by submitting shipping and receiving reports, and on an as-needed basis for personnel-related matters.

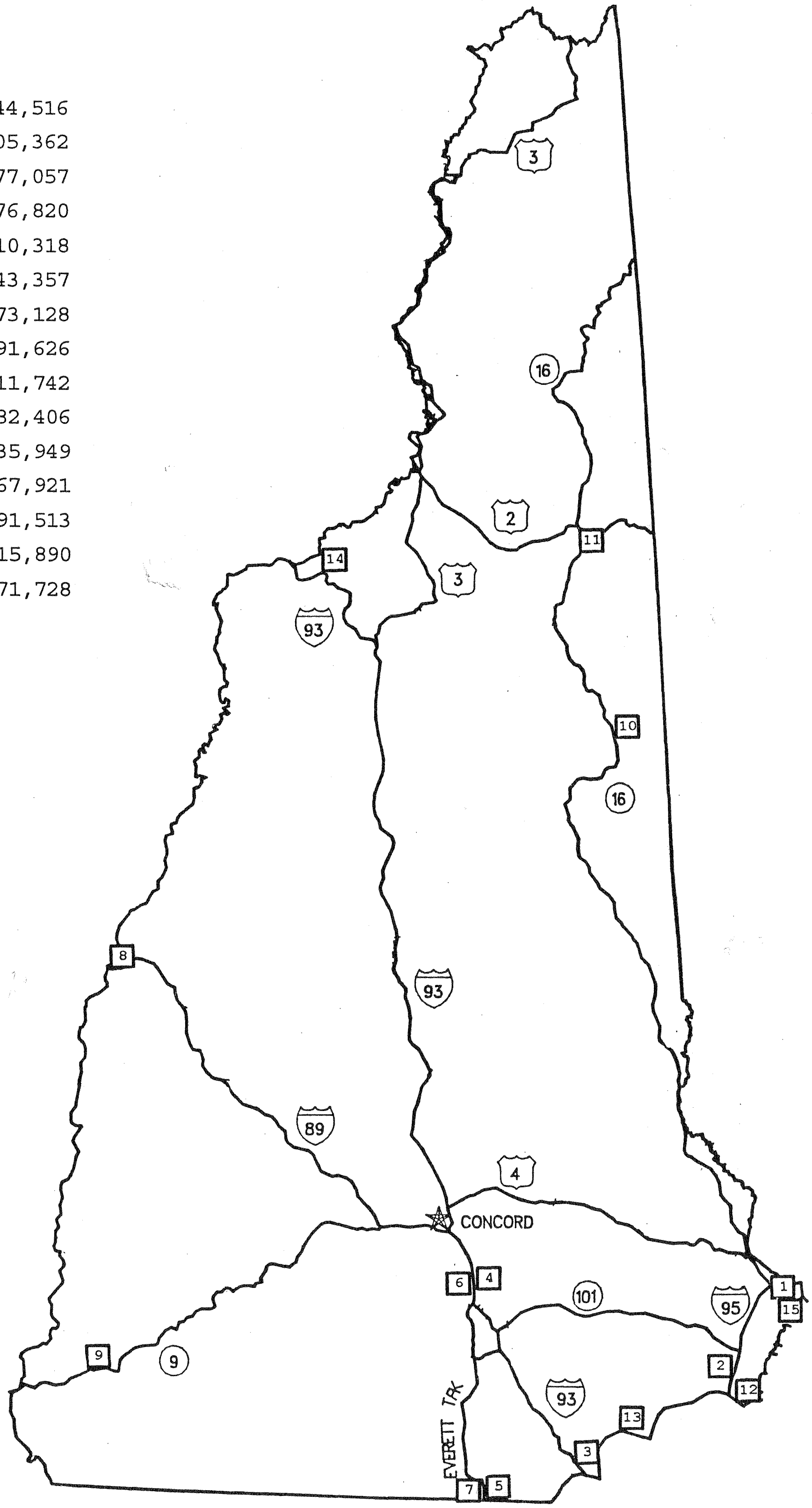
Both the human resources administrator (HRA) and the purchasing agent were reported to be supervised by the financial management director. The HRA is a personnel expenditure through the commissioners' office but they reported transferring the supervisory responsibility for that position. The purchasing agent reported having very little interaction with the financial management director and being supervised directly by the commissioners.

STATE OF NEW HAMPSHIRE
STATE LIQUOR COMMISSION

LOCATIONS OF TOP 15 STATE STORES
(1993 SALES)

FIGURE 3

	Store	Sales
1	Portsmouth (Traffic Circle)	$18,244,516
2	Hampton	$11,205,362
3	Salem	$ 9,577,057
4	Hooksett (North)	$ 7,776,820
5	Nashua (Coliseum Ave)	$ 7,610,318
6	Hooksett (South)	$ 6,843,357
7	Nashua (Southgate)	$ 6,673,128
8	W. Lebanon	$ 6,391,626
9	Keene	$ 4,311,742
10	Conway	$ 4,082,406
11	Gorham	$ 3,835,949
12	Seabrook	$ 3,667,921
13	Plaistow	$ 3,491,513
14	Littleton	$ 3,215,890
15	Portsmouth	$ 2,971,728



1. INTRODUCTION (Continued)

1.2 ORGANIZATIONAL STRUCTURE (Continued)

The SLC employs 305 full-time classified employees plus three unclassified commissioners in its Concord headquarters, warehouse, and 68 stores (Appendix C). As noted earlier, there are seven divisions. These include: (1) marketing and merchandising, (2) purchasing, (3) store operations, (4) warehouse and transportation, (5) financial management, (6) data processing, and (7) enforcement and regulation. The duties and responsibilities of the division directors specified in RSA 176:8 are summarized below.

Marketing and Merchandising

The marketing and merchandising director is responsible for recommending sales to promote competitive position, coordinating in-store promotion with advertising programs, and recommending to the Commission both the delisting of products not meeting gross profit levels and the listing of products that will maximize profits to the State. Gross sales performance for newly listed products are tracked for a three-month test market period in 19 of the State's largest liquor stores. Minimum gross profit, defined by SLC administrative rule Liq 301.03 (j) as the difference between sales dollars and the average purchase order costs, must be $2,200 during the test market period for a product to be listed for full distribution. Products are delisted if sales performance falls below acceptable levels as defined by the Commission. To remain listed, liquor products must make $12,500 and wines $6,500 in gross profits over a continuous 12-month period.

The marketing and merchandising director reported working directly with the contracted advertising consultant to plan and develop advertising concepts and programs. The director also reported working closely with the purchasing agent to ensure product availability and to identify special deals and promotions offered by vendors. Marketing and merchandising coordinates special sales and in-store promotions by working with the store operations director and vendors on in-store marketing and displays. During our performance audit the division had ten full-time employees including the director.

Purchasing

The purchasing agent's responsibilities include assisting the other directors in maintaining levels of inventory within economic limits that meet sales demands, effectively organizing the placement of orders to maintain a balance of receiving workload at warehouses, maintaining a harmonious relationship with suppliers in regard to problems in filling orders on a timely basis, and reporting directly to the Commission. This division has only one employee, the purchasing agent.

1. INTRODUCTION (Continued)

1.2 ORGANIZATIONAL STRUCTURE (Continued)

The purchasing agent works with vendors and stores to maintain warehouse inventory levels. The Commission has set minimum inventory amounts to be kept in warehouses. These amounts are based on comparisons of previous inventory levels at different times throughout the year. The purchasing agent communicates with brokers on a regular basis to discuss monthly inventory needs and any shipment concerns.

Store Operations

The store operations director's statutory responsibilities include recommending changes in store locations and hours, planning store activities to provide maximum customer service, maximizing revenues by promoting the most efficient operation of stores, coordinating the flow of information and reports between the Commission and store managers, and working with the marketing and merchandising director to help formulate and implement the most effective sales, promotional, and marketing techniques. Store operations employed 212 permanent staff during our performance audit. In addition to full-time personnel store operations also uses part-time employees. These employees are restricted to 28-hour work weeks. According to the SLC personnel the part-time employee pool is between 600-800 persons, of which 400-600 are used on a regular basis.

Warehouse and Transportation

The warehouse and transportation division is responsible for developing efficient operating plans for the warehouses, maintaining traffic rate information, developing security measures to minimize loss of inventory, making recommendations to the Commission for improvements in material handling and purchasing, and reporting directly to the Commission. During our audit the division employed 17 permanent full-time employees, including the superintendent.

The SLC owns and operates a warehouse located in Concord and uses space and services in a second, privately-owned, warehouse located in Nashua. Both warehouses operate as bailment facilities, meaning they store product owned by manufacturers and charge monthly fees for storage. The warehouses also charge manufacturers handling and shipping fees.

Financial Management

The financial management director is required to assist the Commission in financial planning, budgeting, and appropriation request preparation. In addition, the financial management director is responsible for installing and maintaining records to assure fiscal and inventory control, maintaining financial records for each store to illustrate operating costs and profitability, and reporting directly to the Commission. The division had 20 employees during our performance audit.

1. INTRODUCTION (Continued)

1.2 ORGANIZATIONAL STRUCTURE (Continued)

The financial management director reported meeting with other division directors to discuss their budgetary needs for appropriation requests and budget preparations. The SLC has its own accounting software program and other programs to track financial information and generate reports. The director reported meeting with the Commission chairman daily to discuss various financial matters.

Data Processing

Data processing is also known as the Management Information Systems (MIS) division. The division director's responsibilities include acquisition, planning, and design for all information systems and data processing, as well as maintaining records to assure fiscal and inventory control, preparing reports as required by the Commission, designing and implementing internal security procedures to minimize losses to the State, gathering and consolidating information for budgetary and other purposes, and recommending to the Commission improvements in the SLC's hardware and software as needed to keep systems current with the industry.

Reports required of the data processing director include results from sales, post-offs, and other promotions, as well as analysis of the profitability of each item listed for sale by the commission. Data processing had 16 employees during our performance audit.

Enforcement and Regulation

The enforcement and regulation chief is responsible for supervising the day-to-day activities of the SLC's enforcement and licensing functions, handling all license applications, and making recommendations, in writing, to the Commission, on whether to grant license applications. Enforcement and regulation had 27 full-time employees during our audit.

Twenty-one investigative personnel geographically located throughout the State are responsible for processing licensing paperwork, enforcing the State alcohol laws, and investigating and prosecuting violators. Investigators typically have caseloads of 200 or more licensees. The director, usually referred to as the chief of the division, reported meeting with the Commission every Monday morning regarding operations in the division, such as disciplinary actions and licensing issues. The chief also reported testifying at legislative hearings and developing division policies and procedures.

1. INTRODUCTION (Continued)

1.3 SCOPE, OBJECTIVES, AND METHODOLOGY

We performed our audit of the New Hampshire State Liquor Commission consistent with recommendations made to the Fiscal Committee by the Legislative Performance Audit and Oversight Committee. This performance audit was conducted in accordance with generally accepted governmental auditing standards and accordingly included such procedures as we considered necessary in the circumstances.

SCOPE AND OBJECTIVES

This report describes and analyzes the organization, management, and control structures of the State Liquor Commission (SLC) during fiscal years 1988 through 1993. Although events that occurred during FY 1994 are in some cases taken into account, the primary focus of this performance audit remains within the identified audit period.

The issues we focused on primarily addressed the structural elements within the SLC, including the internal organization of the agency, management functions within the seven divisions, and management controls in place to ensure the agency's operational efficiency, effectiveness, and economy. Of particular interest within this scope, we examined the operations of the warehouse and transportation system as well as the marketing and merchandising operation.

Our audit encompassed six years of the agency's operation from FY 1988 through the end of FY 1993, and addressed the following specific objectives:

- Assess whether the current organizational structure supports efficient, effective, and economical management;
- Assess current management practices and reporting relationships within the SLC;
- Determine whether the management control structure is sufficient to ensure efficient operations and if the potential for waste, fraud and abuse is minimized;
- Assess the operational efficiency and economy of the warehouse and transportation system; and
- Determine if the marketing and merchandising operations efficiently and effectively fulfill the statutory responsibility to optimize the profitability of the SLC.

1. INTRODUCTION (Continued)

1.3 SCOPE, OBJECTIVES, AND METHODOLOGY (Continued)

METHODOLOGY

To obtain general background information and develop an understanding of the liquor industry nationally, we reviewed reports from performance audits of operations in other liquor control states, as well as articles and research papers published by governmental and non-governmental organizations in the liquor and wine industry including the National Alcoholic Beverage Control Association and the Distilled Spirits Council of the United States.

To obtain background information about the New Hampshire SLC to help design the methodology of our performance audit, we used two basic methods. First, we met with State Legislators, and conducted structured interviews with SLC commissioners and division directors.

Second, we reviewed New Hampshire statutes and administrative rules, past audits and reviews of the SLC, the State's comprehensive annual financial reports, SLC organization charts, SLC reports to the Governor and legislative committees, newspaper articles from 1983-1993, and a 1980 report by two faculty members from Dartmouth College.

To obtain information to accomplish the audit objectives, we used three methods. First, we conducted 84 structured interviews with SLC commissioners and personnel at all levels within the agency, including the warehouse and the stores, as well as with former commissioners and personnel, providers of contracted services, and personnel within other State agencies. Second, we conducted telephone surveys with officials in other liquor control states. Third, we conducted document reviews of federal and state statutes, and internal SLC documents.

1.4 SIGNIFICANT ACHIEVEMENTS

It is important to recognize that performance auditing by its nature is a critical process, designed to identify problems or weaknesses in past and existing practices and procedures. We note here some successful and positive practices, procedures, and programs that we observed and for which sufficient documentation was available.

- STATE LIQUOR AND WINE OUTLET STORES - Many of the State stores have been remodeled to become more pleasant places to shop. In these stores shelves have been updated and replaced, new wine racks have also been installed in some stores, interior signage has been improved, and in-store liquor and wine advertising has been enhanced.

1. INTRODUCTION (Continued)

1.4 SIGNIFICANT ACHIEVEMENTS (Continued)

- INCREASED EMPHASIS ON WINE SALES - Beginning in FY 1992, the SLC began a deliberate effort to increase retail wine sales in its State stores. This effort included educational, as well as merchandising components. Twenty-one stores were designated as wine specialty stores. Wine displays in these stores were improved, as noted above. Printed materials explaining wine types, wine tastings, and wine and food complements were made available at State stores. In addition, a televised wine and food cooking series, as well as a "wine and food tour," both featuring recipes and a chef from one of the State's restaurants were created in conjunction with the SLC's contracted advertising firm.

  Reports prepared by the wine marketing specialist indicated that wine sales increased by $4.3 million in FY 1993 over FY 1992, and by $3.4 million in FY 1994 over FY 1993. In FY 1993 wine sales offset a $0.5 million decrease in spirits sales for the same year, while in FY 1994 wine sales offset a $1.7 million decrease in sales of spirits over the previous year. However, the sales data supporting these reports also indicated that for both years the largest increase in wine sales took place in warehouse sales to licensees. In FY 1993 wine sales from the warehouse increased 13.4 percent, compared to a 2.3 percent increase in retail wine sales. In FY 1994 wine sales from the warehouse increased 7.7 percent, compared to a 3.6 percent increase in retail wine sales.

  Data from a customer origination study by the advertising contractor showed that for the first six months of FY 1994 wines accounted for $2-3 million in sales each month from July 1993 through November 1993, and approximately $3.5 million in December 1993. This performance was second only to sales of all types of whiskeys during the first five months of the fiscal year, and third behind the whiskeys and cordials for December 1993.

1.5 REPORT OUTLINE

The remaining chapters of the report present our analysis of the organization, management functions, and management controls of the SLC. Chapter 2 details our analysis of the SLC organizational structure. Chapter 3 describes management issues in the internal divisions. Chapter 4 examines the management control structure within the agency. Finally, Chapter 5 presents conclusions regarding the current condition of the SLC.

2. ORGANIZATION

The organizational structure of the SLC includes the Office of the Commissioners and seven internal divisions ranging in size from one to 212 full-time personnel (Figure 4). Division directors report directly to and are supervised by one or more of the commissioners. There is no level of management between the commissioners and the divisions, such as an executive director. We observed numerous inadequacies and inefficiencies in the SLC organizational structure, beginning with the three-member Commission, but also including the sales-related divisions, administrative support functions, and enforcement. As a result of our observations, we recommend reorganizing the SLC (Figure 5).

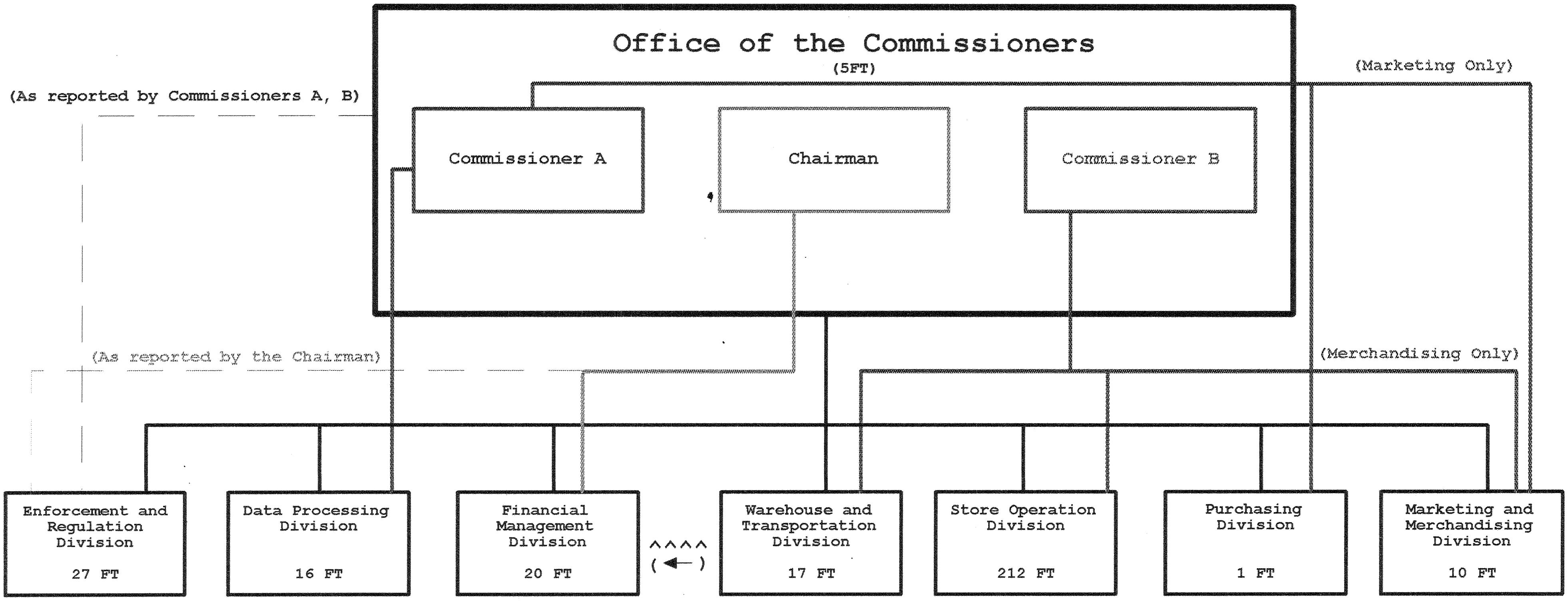
2.1 THE STATE LIQUOR COMMISSION SHOULD BE REORGANIZED

The SLC is one of only two major executive agencies in New Hampshire State government directly headed by three full-time commissioners rather than one (the Public Utilities Commission also has three commissioners but they are primarily involved with hearings and other quasi-judicial regulatory functions, and there is an executive director responsible for day-to-day operations of the Commission). We believe the three-member SLC structure has outlived its usefulness and stands in the way of more streamlined, professional, efficient, effective, and economical organization and management.

In addition, the organization of the marketing and sales structure we observed was inefficient and impeded the SLC's ability to further maximize sales revenue production. Marketing and sales activities for the SLC are carried out in four separately directed divisions: (1) marketing and merchandising, (2) purchasing, (3) warehouse and transportation, and (4) store operations. Although they held different opinions as to how it should be done, each of the directors of the above divisions indicated in their interview responses that some change in the structure of the marketing and sales function would be desirable. Two of the three commissioners indicated no need to change the marketing and sales structure in their interview responses, while the third commissioner supported combining all four divisions. Our analysis of the organizational relationships between these divisions indicated that an integrated structure would improve efficiency and effectiveness in the marketing and sales function.

FIGURE 4

NEW HAMPSHIRE STATE LIQUOR COMMISSION CURRENT ORGANIZATION CHART



LEGEND:

^^^^^ Warehouse and Transportation Superintendent reports to Financial Management Director

Statutory Reporting Relationship

Commissioners' Responsibilities According to Commissioners

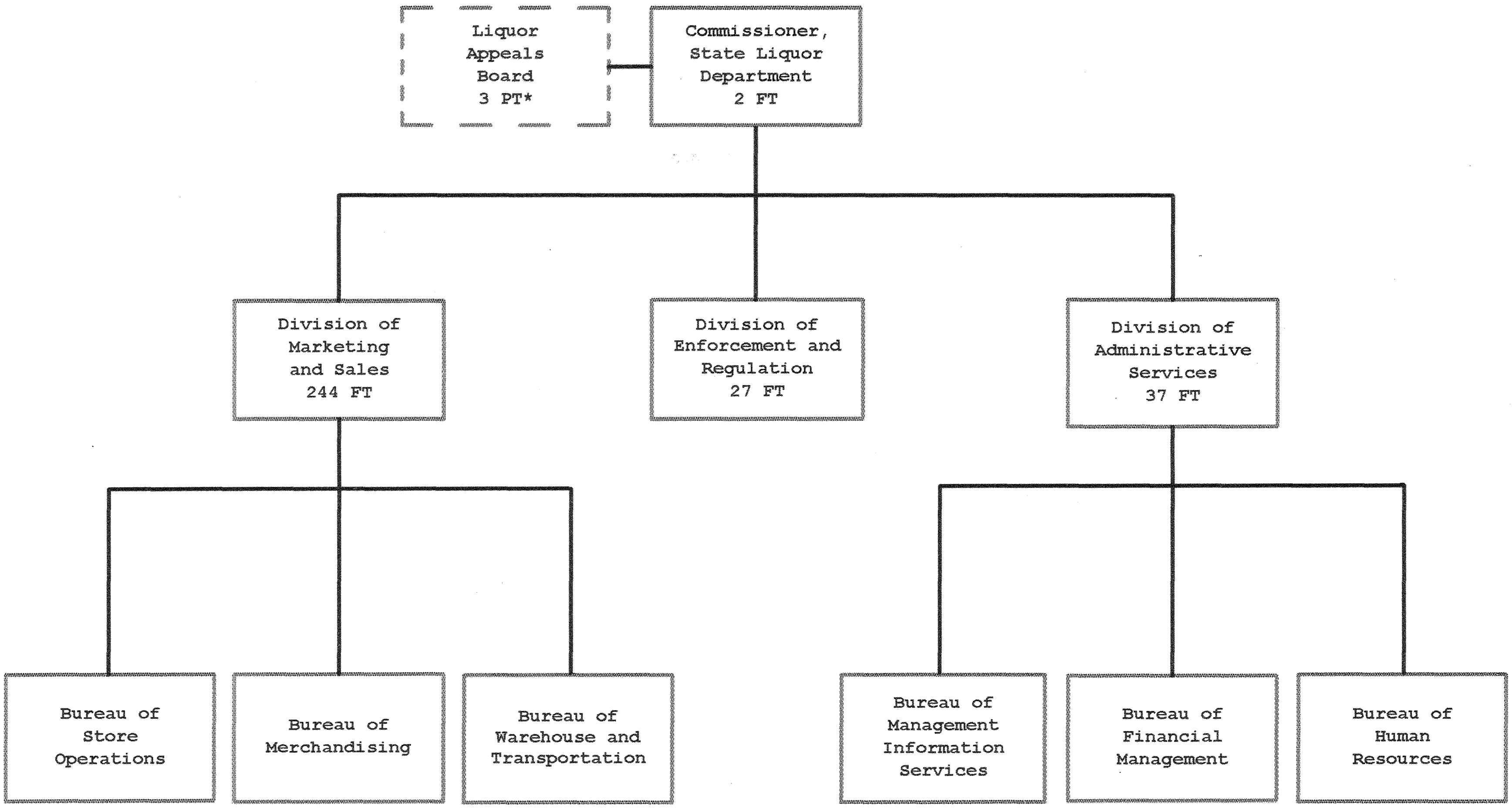
NOTES:

308 TOTAL FULL-TIME EMPLOYEES
FT Full-time employees
INFORMATION CURRENT AS OF 9/16/94

Source: LBA Analysis of State Liquor Commission Data

FIGURE 5

NEW HAMPSHIRE STATE LIQUOR COMMISSION
RECOMMENDED ORGANIZATION CHART



NOTES:

310 FULL-TIME EMPLOYEES
FT Full-time employee
* 3 Part-time board members

Source: LBA

2. ORGANIZATION (Continued)

2.1 THE STATE LIQUOR COMMISSION SHOULD BE REORGANIZED (Continued)

Finally, the organizational structure of the SLC's administrative units does not allow for optimum support and functioning. We observed that the administrative support functions for the entire SLC were performed piecemeal by three different entities: 1) financial management, 2) MIS, and 3) human resources administration. This structure is cumbersome, especially when compared to other executive agencies in New Hampshire that have reorganized under RSA 21-G. For example, the Departments of Corrections, Transportation, Education, and Safety have all included financial management, MIS, and human resources within a single administrative division. Furthermore, we observed unusual reporting relationships within the SLC's administrative services divisions. Additionally, SLC administrative functions had numerous systemic operational inefficiencies.

<u>OBSERVATION NO. 1: THE SLC SHOULD BE HEADED BY A SINGLE COMMISSIONER</u>

The three-member liquor commission is inefficient, unnecessary, and outdated. Multi-headed boards and commissions are satisfactory in fact-finding and advisory capacities, but for purely administrative work they all too often result in divided authority and indecision where efficient and effective coordination and implementation of policy are needed. In addition, matters of a nature that can arguably be said to require multiple decision-makers to ensure fairness, such as listing and delisting products and whether to suspend licenses or fine their holders, require considerably less of the commissioners' time than seems necessary to support three full-time senior officials. The commissioners reported spending from one to three hours weekly adjudicating enforcement issues, plus three to four hours of preparation time.

Examples of inefficient and ineffective management at the three-member SLC include the payment of approximately $246,000 in salary and benefits for three full-time commissioners; lack of adequate policies and procedures in such key areas as financial management, warehouse and transportation, and MIS; and failure to address shortcomings within the organizational structure of the SLC, particularly in the administrative and marketing and sales functions. Most seriously, and as reported in Section 4, there is a lack of effective management controls as evidenced by waste and abuses in personnel administration, purchasing, the advertising contract, and bailment activities.

Public administration literature has documented in state after state and on the federal level the rise in the early part of this century and the subsequent fall of the popularity of commission-type governance. For example, in 1935 a three-member bipartisan commission was chosen to administer the federal Social Security program, but within ten years the

2.1 THE STATE LIQUOR COMMISSION SHOULD BE REORGANIZED (Continued)

OBSERVATION NO. 1: THE SLC SHOULD BE HEADED BY A SINGLE COMMISSIONER (Continued)

commission board was replaced by a single commissioner. In New Hampshire, State agencies headed by boards and commissions were once the norm, but are now the exception. The three-member liquor commission was established in 1933 and has remained essentially unchanged since that time.

The Executive Branch Reorganization Act of 1983 (RSA 21-G) through its declaration of findings and policy as well as its guidelines for reorganization has spelled out the Legislature's desire to now structure the executive branch "...[T]o improve the coordination and management of State services by establishing clear lines of authority, responsibility, and accountability for program implementation...." As indicated above, we observed several reasons why the policy and objectives of the Legislature expressed in RSA 21-G also should be applied to the SLC; particularly the perspective that the organization of State government should assure efficient, effective, and responsive administration.

RECOMMENDATION:

The SLC should be reorganized under the executive direction of a single commissioner pursuant to RSA 21-G. Also, a part-time board comprised of three or five citizen members should be established and administratively attached to the SLC. This board would hear appeals from administrative decisions of the SLC commissioner in matters such as licensing and enforcement, bailment operations, and listing and delisting of products.

AUDITEE RESPONSE:

The SLC does not concur. For the complete text of the SLC's response, see Appendix D, page D-1.

OBSERVATION NO. 2: THE MARKETING AND SALES FUNCTIONS SHOULD BE REORGANIZED

Management and supervisory employees in the four marketing and sales-related divisions report directly to either one or more of the SLC commissioners, another division director, or both a division director and one or more commissioners. For example, one commissioner is more or less responsible for store operations and merchandising and shares responsibility for the warehouse and transportation division with the financial management director. Another commissioner is responsible for marketing and purchasing.

However, no single manager - commissioner or division director - is responsible for the daily, overall coordination of SLC marketing and sales activities and management of the sales-related divisions.

The SLC's ability to meet its statutory requirements regarding profit and customer service is contingent upon its ability to efficiently and effectively coordinate the activities of the marketing and sales-related divisions. The key to the marketing and sales process is the director of marketing and merchandising who is responsible for sales promotions, mark-up recommendations, advertising, and listing and delisting of products. The purchasing director purchases liquor and wines for the system, while product is sold through store operations. Sales promotions necessitate product purchases, so the director of marketing and merchandising must coordinate these purchases with the purchasing director. Product purchased is warehoused and then transported to stores both in anticipation of sales and in response to customer demand. The director of marketing and merchandising must be apprised of product arrivals, product levels in warehouses and stores, and product distribution. The director must coordinate sales promotions with store operations and advertising programs to maximize SLC profitability. The store operations director must see that sufficient product is on hand to support advertised promotions with in-store displays and shelf facings. Timely reports from stores of consumer reaction to sales promotions, pricing, and product availability enables the marketing and merchandising director to analyze product and promotional performance and begin the process over again.

Operational inefficiencies occurring within the sales-related divisions have caused product shortages and outages during peak holiday sales seasons. Due to difficulties maintaining store and warehouse inventory levels, customers in the past have sometimes been unable to make certain purchases. Store division personnel also reported warehouse stock outages occur throughout the year. Store division personnel stated that stores sometimes received insufficient notification of upcoming sales. One store manager reported that six times over the course of a year product could not be ordered in time for sales due to insufficient notification.

According to personnel within the four divisions, the mix of reporting relationships, lack of effective coordination, and differing management styles have caused conflicts to arise which were serious impediments to more efficient SLC operations. For example, personnel reported problematic communication including conflicting directives and serious differences of opinion regarding such basics as inventory levels in stores.

OBSERVATION NO. 2: THE MARKETING AND SALES FUNCTIONS SHOULD BE REORGANIZED (Continued)

The Executive Branch Reorganization Act of 1983 (RSA 21-G) requires that organization of State government assure efficient, effective and responsive administration. The act also requires the establishment of clear lines of authority, responsibility and accountability in order to improve coordination and management of State services. Although not "reorganized" under RSA 21-G, the SLC is nonetheless similarly required to optimize profitability, maintain proper controls, assure effective and efficient commission operation, and provide service to customers (RSA 176:3(I-IV)).

The SLC has not adequately analyzed the weaknesses of the organizational structure for its marketing and sales functions. It has assigned supervisory responsibilities in a haphazard manner, sometimes for reasons other than organizational efficiency. For example, on paper the purchasing agent and the warehouse superintendent report to the financial management director. In reality the financial management director does not provide an acceptable level of supervision for the purchasing agent or the warehouse superintendent. According to the commissioners those reporting assignments were designed in an attempt to influence an upgrade of the financial management director's position.

RECOMMENDATION:

The SLC's four sales-related divisions - marketing and merchandising, purchasing, warehouse and transportation, and store operations - should be reorganized into one sales and marketing division. There should be a director of sales and marketing supervising separate bureaus for merchandising, warehouse and transportation, and store operations. This reorganization should be implemented without the necessity for additional personnel.

AUDITEE RESPONSE:

The SLC concurs in part. For the complete text of the SLC's response, see Appendix D, page D-5.

OBSERVATION NO. 3: ADMINISTRATIVE FUNCTIONS SHOULD BE REORGANIZED

The SLC reported that one commissioner was responsible for overseeing the MIS division, while a second commissioner oversaw financial management. The human resources administrator position, while budgeted within the office of the commissioners, was reportedly supervised by the three commissioners and

OBSERVATION NO. 3: ADMINISTRATIVE FUNCTIONS SHOULD BE REORGANIZED (Continued)

the financial management director. However, no single manager - commissioner or division director - was responsible for the daily, overall coordination of SLC administrative functions. Operational inefficiencies occurred within administrative units and unclear lines of authority existed. The SLC has not adequately analyzed weaknesses in the organizational structure for its administrative functions. It has assigned supervisory responsibilities in a haphazard manner, sometimes for reasons other than organizational efficiency. As noted in the introduction, the human resources administrator reports to the financial management director. In reality the financial management director does not provide an acceptable level of supervision for the human resources administrator.

RECOMMENDATION:

Three administrative-related units - financial management, MIS, and human resources administration - should be reorganized into one administrative services division. There should be a director of administrative services supervising separate bureaus for financial management, MIS, and human resources administration. This reorganization should be implemented without the necessity for additional personnel.

AUDITEE RESPONSE:

The SLC concurs in part. For the complete text of the SLC's response, see Appendix D, page D-7.

2.2 STORE OPERATIONS

Store operations, which is the retail component of the marketing and sales function, consists of 68 State liquor and wine outlet stores. In FY 1993, retail sales accounted for over $157 million, or 75.3 percent, of the SLC's total sales. Due to the number of stores and personnel employed in them, it is necessary that stores have an organizational structure that assures sufficient supervision, management and accountability. The organizational structure we observed did not provide the needed assurances.

2. ORGANIZATION (Continued)

2.2 STORE OPERATIONS (Continued)

OBSERVATION NO. 4: THE SUPERVISOR/MANAGER SYSTEM SHOULD BE REPLACED

The store operations director and 11 supervisor/managers provided supervision for the store operations division. Supervisor/managers were responsible for both managing one store and supervising the operations of from one to ten other stores. The supervisor/manager system was devised in the late 1980s to reduce operating costs. Supervisor/managers and managers reported shortcomings in the system in their interview responses. Also, our survey of other control states and private businesses did not disclose use of the supervisor/manager system anywhere else.

Supervisory duties of supervisor/managers included monitoring store marketing and merchandising activities, auditing store inventory and financial data, and investigating all shortages. Supervisor/managers managed stores requiring retail store manager IIs to retail store manager IVs; all store supervisor/managers were capable of performing as retail store manager IVs. Duties of the retail manager IV included supervising assistant managers and a large staff of store employees, teaching retail store operations to store employees, studying sale trends and adjusting inventory reorder figures, and reviewing reports of subordinate staff regarding cash receipts, bank deposits, voided transactions, inventory control and sales trends.

Of the 11 supervisor/managers, only nine actually performed the supervisor/manager function. Two supervisor/managers were performing other duties at the main SLC office in Concord instead. One supervisor/manager worked full-time on the shelf management program within the Management Information System Division. The other supervisor/manager served as acting director of store operations while the position was vacant and as full-time assistant director of stores at other times. The stores that these two supervisor/managers supervised were reassigned to two other supervisor/managers. (In Observation No. 18, we recommend these two positions be returned to service as district supervisors or store managers.)

The 1987 Sunset Report recommended that the SLC analyze the supervisor/manager system. The SLC has not conducted such analysis. The chairman reported changes in the supervisor/manager system would depend on electronic communication development, while another commissioner saw nothing wrong with the current system.

Comments from SLC store division personnel indicated several problems with the supervisor/manager system. According to SLC store supervisor/managers and managers, the supervisor/managers frequently were unable to manage their own store and supervise other State liquor stores effectively. For example, three supervisor/managers reported not having time to supervise other stores during the peak busy periods, which is the most important time for such supervision. Even under normal conditions, supervisor/managers stated they

OBSERVATION NO. 4: THE SUPERVISOR/MANAGER SYSTEM SHOULD BE REPLACED (Continued)

were spread too thin, were unable to do much fine-tuning and merchandising, and had to ensure adequate coverage in their own store when out supervising other stores. Store supervisor/managers are supposed to visit stores they supervise every two weeks, yet this was not always accomplished. According to store division personnel, supervisor/managers and managers met only once every three to four weeks, although they talked more frequently by telephone.

In addition, no store supervisor/managers reported performing required periodic store audits. The SLC store operations director stated that current SLC auditing functions were insufficient, and that store cash operations needed considerable improvement, including accountability trails to prevent employee theft.

Three former SLC commissioners commented they were wrong to support the supervisor/manager system. One former commissioner reported that although he did not like to criticize the system because he put it together, he never observed any benefits. The system did not work because it could not ensure both sufficient management in the supervisor/manager's own store, and sufficient supervision of the other stores. In this former liquor commissioner's opinion, SLC supervisors should supervise full-time instead of having store responsibilities. Another former commissioner reported that the commissioners made a mistake supporting the supervisor/manager system, and that it was especially poor for a supervisor/manager to manage a large store. The system should be abolished and replaced with independent personnel conducting supervision of stores, according to this former liquor commissioner. The third former commissioner commented that he was very opposed to impeding supervisory oversight as occurs with the supervisor/manager system. This former liquor commissioner stated that SLC store supervisors needed the freedom to supervise stores and to travel to stores at will.

Out of 17 control states and one control county (Montgomery County, MD), 13 operate stores and five do not. Of the 13 that operate stores, none utilize supervisors that also manage stores. Additionally, none of the New Hampshire non-liquor private retailers we surveyed used a supervisor/manager system. Due to the supervisor/manager system, insufficient supervision of store operations occurs. This leads to store inefficiency and may harm SLC profitability. Insufficient monitoring of store marketing and merchandising activities occurs. Store audits to verify the accuracy of store inventory, reported sales and voids, bank deposits, and related store financial data are not performed as frequently as necessary. This increases the opportunity for fraud and theft, as investigations of cash and inventory shortages may neither be timely nor sufficient.

OBSERVATION NO. 4: THE SUPERVISOR/MANAGER SYSTEM SHOULD BE REPLACED (Continued)

RECOMMENDATION:

The SLC should replace the supervisor/manager system and reclassify six positions as district supervisors who oversee store managers. The SLC should consult with the Division of Personnel to ensure these positions are reclassified pursuant to administrative rules issued by the division. The district supervisors' responsibilities should include supervision, in-service training, and evaluation of store managers and staff. They should report to the store operations administrator, who should ensure that district supervisors remain thoroughly familiar with day-to-day operations of stores. District supervisors might also assist in product transfer between stores, as long as it does not interfere with their supervisory duties. District supervisors should frequently perform both announced and unannounced store visits, including spot audits of cash and inventory.

The number of stores each district supervisor would be responsible for should be determined according to several factors including the following: store geographic location, size, sales volume, and travel time between stores. District supervisors should hold store managers and store employees accountable for store sales, losses, maintaining and reporting proper inventory levels, bank deposits, proper product presentation, store cleanliness, customer relations, and implementing store operations directives. The district supervisors should also review store manager reports for accuracy and timeliness.

After six of the current 11 supervisor/manager positions have been reclassified as district supervisors, the remaining five supervisor/manager positions should be reclassified as store manager positions. The SLC should consult with the Division of Personnel to ensure that these reclassifications, along with salary adjustments, occur according to administrative rules issued by the division. Finally, vacancies in store manager positions necessitated by removing store management responsibilities from supervisor/manager positions should be filled according to Division of Personnel administrative rules.

AUDITEE RESPONSE:

The SLC concurs in part. For the complete text of the SLC's response, see Appendix D, page D-10.

2. ORGANIZATION (Continued)

2.3 ENFORCEMENT AND REGULATION

The Enforcement and Regulation Division is headed by a chief, and contains three levels of supervision. The organizational structure is more complex than the size of the division warrants. We found inadequate supervisory control in field operations, redundancy in other supervisory relationships, and insufficient support for some position classifications.

OBSERVATION NO. 5: ENFORCEMENT AND REGULATION DIVISION ASSISTANT CHIEFS SHOULD NOT HAVE CASELOADS

The chief supervises three assistant chiefs. During the audit field work two of the assistant chiefs were assigned to field operations and the third was responsible for administrative supervision of the licensing and auditing personnel working in the SLC's headquarters. The field assistant chiefs were each assigned half of the state to supervise. (The division reported there were approximately 3,500 active licenses in FY 1993.)

Between 1989 and 1990, due to cutbacks and a hiring freeze, each field assistant chief began to carry a licensing and investigative caseload of between 225 - 280 licensees, as well as supervising eight or nine liquor investigators. The assistant chiefs also assume additional caseloads when division investigator vacancies occur. The enforcement and regulation chief reported licensing caseload assignments for the two field assistant chiefs were necessary due to an insufficient number of investigators. This arrangement has allowed the assistant chiefs to perform only rudimentary supervision, such as reviewing paperwork and weekly activity reports. We question how much substantive supervision is possible with this arrangement, and whether lack of adequate supervision could present a potential for legal liability to the State.

One assistant chief reported being unable to directly observe investigative personnel apart from checking their reported weekly activities and reviewing their paperwork. The second assistant chief reported having significantly less time for supervisory responsibilities since his licensing caseload had to take priority over supervising investigators. This assistant chief also reported that investigators inform him as to their activities, yet at times fail to contact him when problems occur. The second assistant chief further commented that his supervisory and investigatory duties require that he work up to 180 hours or more per 28-day cycle.

Several investigators reported that the assistant chiefs' caseloads made it difficult to have face-to-face meetings. One investigator reported not seeing his assistant chief for eight to nine months, while another reported a period of two to three months. Other significant comments by division personnel included:

OBSERVATION NO. 5: ENFORCEMENT AND REGULATION DIVISION ASSISTANT CHIEFS SHOULD NOT HAVE CASELOADS (Continued)

- supervisor is tied up with work that should be done by investigators,
- don't see supervisor too often due to area he covers, and
- lack of periodic supervision leads to lines being crossed by investigators.

Organizational literature defines direct supervision as a basic element of structure and "a glue" that holds organizations together. Direct supervision means one individual taking responsibility for the work of others, issuing instructions, and monitoring actions. Direct supervision is the fundamental way that organizations coordinate work. Effective supervision is compromised by requiring supervisory personnel to carry full licensing caseloads. The assistant chiefs must have the freedom to conduct adequate supervisory oversight.

RECOMMENDATION:

The two field assistant chiefs should not carry a caseload of licensees. Their primary responsibilities should be supervising subordinate liquor investigators by (1) ensuring liquor investigators remain thoroughly familiar with liquor licensing and enforcement laws and regulations, (2) assisting subordinates with non-routine or dangerous investigations, (3) orienting new personnel, and (4) helping ensure subordinate division staff meet training requirements. (We have elsewhere recommended that the administrative assistant chief and the senior investigator/training officer return to the field to carry licensing and investigative caseloads. These two personnel should be able to assume the caseloads of the field assistant chiefs.)

AUDITEE RESPONSE:

The SLC concurs in part. For the complete text of the SLC's response, see Appendix D, page D-14.

OBSERVATION NO. 6: THE ADMINISTRATIVE ASSISTANT CHIEF POSITION IS UNNECESSARY

The third assistant chief worked in an administrative capacity at the commission's central office during audit field work. The administrative assistant chief did not carry an investigative caseload and did not supervise field investigators. The position creates a redundant level of management and extra expense within the SLC. The administrative assistant

2. ORGANIZATION (Continued)

2.3 ENFORCEMENT AND REGULATION (Continued)

OBSERVATION NO. 6: THE ADMINISTRATIVE ASSISTANT CHIEF POSITION IS UNNECESSARY (Continued)

chief was performing supervisory duties that supplemental job descriptions required of the examiner II and the administrative secretary/supervisor, and that have been performed by these two positions.

The administrative assistant chief reported a typical work week involved responding to calls from the field, filling in when the chief was out, drafting administrative rules, memo writing, correspondence, proofing the weekly enforcement agenda, and supervising the administrative and audit staff. The administrative assistant chief also reported that the administrative secretary/supervisor supervised and conducted performance evaluations for two clerical positions and the account technician in the administrative section, as well as managing day-to-day office operations and processing license applications. The administrative assistant chief also reported being responsible for coordinating investigator training. However, the division also had a senior investigator responsible for education and training concerns. In addition, the administrative assistant chief reported having spent approximately 30 percent of his time during the previous two years writing an investigator manual.

According to the Division of Personnel, the administrative assistant chief's duties were formerly required of a deputy chief. The deputy chief position became vacant due to promotion in February 1991. The current administrative assistant chief was promoted from senior investigator in May 1991. The Division of Personnel reduced the position's labor grade and reclassified the position to assistant chief in June 1992.

The administrative assistant chief's job description requires the position to: (1) supervise liquor commission investigators and administrative staff; (2) draft, analyze and interpret proposed training manuals; (3) "plan, evaluate and implement in-service training" for all division personnel; (4) appear before legislative committees; (5) "monitor and supervise all work activities performed" by division personnel; and (6) direct the division when the chief is on leave.

The supplemental job description for the administrative secretary/supervisor requires the position to perform the following: (1) supervise office personnel, (2) perform administrative secretarial activities, (3) assist MIS in formulating/implementing new programs or changes pertaining to the division, and (4) provide educational enforcement information to licensees and others.

OBSERVATION NO. 6: THE ADMINISTRATIVE ASSISTANT CHIEF POSITION IS UNNECESSARY (Continued)

The supplemental job description for the examiner II requires the position to supervise the activity of the auditing section including: (1) review and approve work schedules, audit findings and reports, reports of violation recommending punitive action, leave, travel, and vehicle use; (2) review reports and summaries prepared by the account technician; and (3) take disciplinary action and recommend hiring new employees for auditing.

Specialists in the Division of Personnel reported that the administrative assistant chief position was not needed in order to cover supervisory functions. Division of Personnel staff reported that the examiner II and the administrative assistant chief were the same labor grade and step and did not recommend having one employee supervise another employee with an identical labor grade. Division of Personnel management also stated that the position of administrative assistant chief was unnecessary for a division as small as the Enforcement and Regulation Division. Division of Personnel management further commented that the following should supervise personnel and report to the chief: (1) the administrative secretary/ supervisor, (2) the examiner II, and (3) the two field assistant chiefs. The chief reported that his request to upgrade the administrative assistant chief's position was denied by the Division of Personnel. Division of Personnel management explained the request was denied because the administrative assistant chief's level of responsibility was no different from that of the other assistant chiefs.

Former commissioners also reported the administrative assistant chief position was unnecessary. One former commissioner reported the position should be eliminated or put into the field because it was a waste of money when enforcement had personnel shortages. Another former commissioner reported the administrative assistant chief's responsibilities did not require a full-time assistant chief. Instead, the responsibilities could be covered by rotating officers. This would increase staff knowledge and increase cross-training. In this former commissioner's opinion, if problems were to occur with the chief, there would be 15 officers available to fill the void.

RECOMMENDATION:

The SLC should reclassify the position of administrative assistant chief to an additional liquor investigator position. The SLC should consult with the Division of Personnel to ensure this position is reclassified pursuant to administrative rules issued by the Division.

2. ORGANIZATION (Continued)

2.3 ENFORCEMENT AND REGULATION (Continued)

OBSERVATION NO. 6: THE ADMINISTRATIVE ASSISTANT CHIEF POSITION IS UNNECESSARY (Continued)

AUDITEE RESPONSE:

The SLC does not concur. For the complete text of the SLC's response, see Appendix D, page D-16.

OBSERVATION NO. 7: THE SENIOR LIQUOR INVESTIGATOR LABOR GRADE IS NOT NEEDED

We observed that the senior liquor investigator position required performance of duties almost identical to those of liquor investigators. Both positions were required to enforce liquor laws, investigate possible liquor violations, educate and relicense current licensees, and license new applicants. Senior liquor investigators were also responsible for supervising investigator trainees. However, interview responses from enforcement personnel indicated senior liquor investigators rarely supervise trainees. We question the need for the senior liquor investigator classification.

The senior liquor investigators' supplemental job description lists several supervisory responsibilities:

- coordinate and direct a team of liquor investigators to conduct enforcement investigations;
- supervise and evaluate work of subordinate investigators to provide investigative strategies and technique; and
- train new liquor investigators on departmental procedures, regulations and licensing problems so as to become proficient in their duties.

The enforcement chief reported that senior liquor investigators did not normally have supervisory responsibilities apart from supervising new investigators in training. Other investigative staff agreed, including two of the four senior investigators working in the field. As reported earlier, another senior investigator worked in the SLC's Concord office (as well as out of his home like other investigators) and was assigned to coordinate training and education for the division. This investigator also was assigned to maintain licensee files in the Concord office one to two days per week.

OBSERVATION NO. 7: THE SENIOR LIQUOR INVESTIGATOR LABOR GRADE IS NOT NEEDED (Continued)

Because the current senior investigator supplemental job description has not been revised to reflect the position's actual, diminished duties, the State is spending more on salaries for senior investigators than is necessary.

RECOMMENDATION:

The senior liquor investigator classification should be abolished in accordance with Division of Personnel rules. The current positions of senior investigator should be reclassified to liquor investigator positions. Responsibility for orienting new investigators should be shifted to the assistant chiefs. Responsibility for coordinating training and education for investigators and other division personnel should be the responsibility of a centralized SLC training officer.

AUDITEE RESPONSE:

The SLC does not concur. For the complete text of the SLC's response, see Appendix D, page D-21.

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STATE OF NEW HAMPSHIRE
STATE LIQUOR COMMISSION

MANAGEMENT FUNCTIONS

3. MANAGEMENT FUNCTIONS

Problems with the SLC's fractionalized organizational structure translate into management problems in key functions. Areas of concern include planning in the marketing and sales function, warehouse safety, MIS planning and support, human resources including staff training, and others. These problems serve to weaken SLC operations, negatively impacting their efficiency and effectiveness, and diminishing the SLC's ability to optimize profits and contribute to State revenues. By statute the commissioners possess ultimate accountability for effective and efficient SLC operations.

3.1 MARKETING AND SALES

The marketing and sales function is the largest revenue producer for the SLC and integral to meeting the commission's statutory requirement to optimize profitability (RSA 176:3 (I)). The four divisions primarily involved in the function, marketing and merchandising, stores, purchasing, and the warehouse, employ 240 of the SLC's 308 full-time personnel (77.9 percent). To ensure maximum attainment of its statutory mandate, as well as to provide adequate management of employees, some improvements in marketing, planning, store staffing, and warehouse operations are required.

OBSERVATION NO. 8: MARKET PLANNING PROCESS SHOULD BE IMPROVED

A function of marketing management is knowing and reacting to critical changes in markets, technologies, and methods for reaching and communicating with markets. This marketing concept presses businesses to develop marketing and merchandising plans, a tool by which they implement strategic commerce, with anticipated consequences (revenue production), over a specified period of time. Deviations from expected results, changes in market conditions (including competition), and merchandising innovations all propel business to re-tune their marketing and merchandising plans at least annually if not earlier. We observed that the SLC plan was not revised regularly to reflect conditions identified above.

The SLC marketing and communications plan was developed to identify the "general marketing and communications strategy" over the three-year period FY 1993 - FY 1995. The introduction to the marketing and communications plan disclaimed its purpose as substituting for a "tactical marketing outline" prepared by commission staff. However, marketing personnel were unable to provide us with the tactical marketing outline. Therefore, the marketing and communications plan appeared to be the commission's only formal marketing and merchandising plan.

3. MANAGEMENT FUNCTIONS (Continued)

3.1 MARKETING AND SALES (Continued)

OBSERVATION NO. 8: MARKET PLANNING PROCESS SHOULD BE IMPROVED (Continued)

Marketing and merchandising plans are designed to provide specific guidelines for conducting business over a specified period of time, yet should remain flexible and responsive for modification in the face of market changes and merchandising innovations. Formal short term planning cycles, which result in a document that is written and circulated to all key players in the organization help to ensure those players are informed of business goals and objectives, as well as their roles in meeting those objectives. Marketing literature identifies the need for annual planning cycles, as well as shorter term tactical planning. Marketing audits typically evaluate development of marketing plans on an annual basis as performance criteria. The marketing and merchandising plan was in its third year during our performance audit. There had been no revisions or updates to the plan during its three-year implementation. According to the advertising agency, the plan was intended to be a three-year document. The commission had not asked the advertising contractor for any revisions.

Marketing plan development also should include input from the entities that contribute to the marketing function. The SLC's marketing and merchandising plan was conceived amid turnover in marketing and sales management, and with limited or no input from key divisions including store operations, the warehouse, and MIS. Furthermore, the advertising contractor has taken the lead in providing data to the SLC due to limited MIS involvement in the marketing planning process, thus reducing available advertising funds. We are concerned sufficient input was not solicited in developing, writing, and updating the SLC marketing plan.

Development of the three-year marketing plan was done by the commissioners and the advertising contractor with limited input from the divisions. Conflicting reports among various sources prevented us from identifying exactly who else may or may not have been involved in the process. Commissioners in office at the time related different versions of the plan's development and of SLC personnel involvement.

The MIS director reported having no input into the plan. The advertising agency consultant acknowledged this but reported receiving regular assistance from the data processing project manager regarding specific marketing needs.

A marketing committee comprised of the directors of marketing, stores, and purchasing, along with the wine specialist and the public information specialist meet on a weekly basis with representatives from the advertising contractor. The committee plans and discusses upcoming sales and promotions, as well as advertising concepts to support them. This committee appears to be the entity within the SLC nearest to the marketing and merchandising strategy.

OBSERVATION NO. 8: MARKET PLANNING PROCESS SHOULD BE IMPROVED (Continued)

An efficient and effective marketing and sales operation requires planning, coordinating, and evaluating marketing and merchandising promotions. MIS involvement throughout the process should be integral. Target market research, analyses of past performance, and sales projections are three examples where MIS expertise is needed to support data collection and analysis. Limited MIS input into the marketing planning process has meant the advertising contractor has had to take the lead in providing data to the SLC. Analysis of a zip code survey was sub-contracted through the advertising budget, reducing by $15,000 the funds available in FY 1994 for advertising uses.

RECOMMENDATION:

The SLC should ensure continuous review and yearly, formal updates to the marketing and merchandising plan. Developing, writing, and updating the marketing plan should be the responsibility of marketing and sales related personnel. All marketing and sales management personnel, as well as top MIS management, should participate in marketing planning activities.

AUDITEE RESPONSE:

The SLC concurs in part. For the complete text of the SLC's response, see Appendix D, page D-26.

OBSERVATION NO. 9: ADVERTISING BUDGET SHOULD BE REVIEWED

The SLC uses advertising to inform customers of sales promotions in the hopes of increasing profits and thus revenues for the State's general fund. Personnel from marketing and merchandising and the advertising agency reported the amount of the advertising contract was small compared to the gross profit generated by the SLC. At $606,761 in FY 1993, the SLC's advertising expenditures were 0.29 percent of its $208.6 million in gross revenues. Advertising budgets of two to three percent of gross revenues are reportedly typical in most private sector businesses.

The Sweepstakes Commission's advertising contract during FY 1993 was 180 percent higher than the SLC's advertising contract. By comparison, the Sweepstakes Commission operating income was only 89 percent of the SLC's operating income in FY 1993.

OBSERVATION NO. 9: ADVERTISING BUDGET SHOULD BE REVIEWED (Continued)

The SLC has had few objective methods to evaluate its advertising expenditures. Coded newspaper coupons were being developed and direct mail efforts were recently initiated according to the advertising contractor. Data from the zip code survey collected through the first six months of FY 1994 supported the concentration of newspaper advertising in two Massachusetts counties contiguous to the State border. Support for radio advertising from Boston broadcast stations was not clearly demonstrated in the zip code survey. Boston-based radio stations in FY 1992 accounted for 80.8 percent of all SLC radio expenditures, while in FY 1993 they accounted for 82.7 percent.

Advertising agency representatives reported concerns with the size of the advertising budget, stating that as advertising costs increase there will be a decrease in the SLC's media purchasing power. Additional advertising funds would also allow for more research, according to the advertising agency.

RECOMMENDATION:

The SLC should conduct an effectiveness review of its advertising budget. Expenditures for media placements and production, as well as for market research activities should be analyzed. Whenever possible, expenditures for research-related functions should be targeted for future budgeting in the SLC's marketing and sales units.

AUDITEE RESPONSE:

The SLC concurs in part. For the complete text of the SLC's response, see Appendix D, page D-29.

OBSERVATION NO. 10: STORE STAFFING SHOULD BE REVIEWED

The SLC sells alcoholic beverages chiefly through the 68 State liquor and wine outlet stores. Sufficient store staffing helps the Commission fulfill its statutory obligations to maximize profits and provide service to customers. Finding the proper balance in staffing can be difficult, however. While excessive staffing drains finite SLC store payroll resources, insufficient store staffing can present myriad difficulties and translate into State revenue drains due to pilferage and inadequate customer service. Likewise, the mix of full-time and part-time staffing is equally important. Full-time employees must be paid benefits yet represent a generally stable and experienced workforce. Part-time employees relieve

OBSERVATION NO. 10: STORE STAFFING SHOULD BE REVIEWED (Continued)

benefit expenditures, which may stress the operating budget for store operations, but may lack the same level of commitment and knowledge possessed by full-time employees.

According to store operations personnel, staffing levels are inadequate. Three of four supervisor/managers and five of seven managers we interviewed stated there were problems in acquiring sufficient part-time, temporary help. Some stores conduct business with just one employee in the store. Division management stated that small stores are open an average of 53 hours per week with two full-time permanent employees. A supervisor/manager stated that during peak periods security surveillance of customers was impossible because of too few employees. This increases the risk of customer theft. The director of store operations stated that for security purposes no store should ever operate with fewer than two employees.

The SLC chairman reported that store personnel levels were reduced from 400 full-time employees to under 200. Full-time positions were replaced by part-time personnel at lower rates of pay and without benefits. The chairman further stated that current store staffing is so lean that, against the best interests of the State, part-time personnel are opening and closing some stores.

Total Store Operations Division personnel expenditures decreased in FY 1991 and FY 1992. FY 1991 expenditures decreased seven percent from FY 1990, while FY 1992 expenditures decreased five percent over FY 1991. Since FY 1992, total personnel expenditures have risen (three percent in FY 1993 and 0.13 percent in FY 1994.) However, it is difficult to conclude how much of the difference in total expenditures is due to reduced use of full-time employees because five stores were closed in FY 1991 and four stores were closed in FY 1992 (one store that was closed in FY 1991 was reopened in FY 1992).

The level of funding necessary to support an adequate number of temporary store employees may have been under-estimated. Analysis of division personnel expenditures shows that in FY 1992 more than $76,000 of $2.25 million in appropriated funds for part-time personnel (class 50 funds) lapsed. For FY 1993, only $300 of $2.33 million in appropriated class 50 money was allowed to lapse. For FY 1994, the SLC's class 50 expenditures were $2,448,000, exceeding the initial FY 1994 class 50 appropriation of $2,351,000 by $97,000. Insufficient store staffing levels may encourage customer and employee theft and increase risk for store employees. Store division personnel stated that current staff levels jeopardize employees making bank deposits safely while leaving sufficient personnel to adequately perform store operations. Additionally, a supervisor/manager commented that it was dangerous for store employees to work alone at night. This

OBSERVATION NO. 10: STORE STAFFING SHOULD BE REVIEWED (Continued)

supervisor/manager preferred employees, when necessary, to work alone in the morning. The store operations manual requires two employees to close stores - one to close and lock all doors and windows and a second employee to double-check the secureness of each door and window.

RECOMMENDATION:

The SLC should review store staffing levels to determine if they are sufficient.

AUDITEE RESPONSE:

The SLC concurs. For the complete text of the SLC's response, see Appendix D, page D-33.

OBSERVATION NO. 11: SLC SHOULD ASSESS COSTS AND BENEFITS OF A ONE-WAREHOUSE OPERATION AND PUT LICENSE FOR PRIVATELY-OWNED WAREHOUSE OUT TO BID

The Warehouse and Transportation Division receives, stores and distributes alcoholic beverages to State liquor and wine outlet stores and licensees throughout the state. SLC storage space requirements exceed its Concord warehouse's available space. Approximately 200,000 square feet of space is used to store alcoholic beverages. The Concord warehouse has approximately 60,000 square feet of storage space. For the past 24 years the SLC has used a privately-owned warehouse in Nashua as a second distribution center. In addition to the privately-owned warehouse which is used on a continual basis, the SLC uses another location in Concord during peak sale months.

Multiple storage facilities are not an efficient use of limited State resources and do not efficiently and effectively distribute alcoholic beverages to State stores or licensees. Lack of a centralized distribution system means the SLC pays duplicative expenses for freight and handling.

We identified two areas where duplicate expenses may be reduced or eliminated through the use of one warehouse. First, for FY 1988-FY 1993 the SLC paid approximately $427,000 in additional delivery costs to ship from the Nashua warehouse to State stores. According to SLC warehouse personnel, these additional charges were due to the smaller loads shipped from the Nashua warehouse which increase the delivery cost per case. In addition, warehouse management spends more time scheduling deliveries from two warehouses.

OBSERVATION NO. 11: SLC SHOULD ASSESS COSTS AND BENEFITS OF A ONE-WAREHOUSE OPERATION AND PUT LICENSE FOR PRIVATELY-OWNED WAREHOUSE OUT TO BID (Continued)

Second, for FY 1988-FY 1993 the SLC paid $1.1 million for services provided by the Nashua warehouse, for an average expense of $186,681 per fiscal year. Those services included product storage, handling, shipping, and other miscellaneous charges such as telecommunication costs. The cost of those services ranged from a high of $240,450 in FY 1988 to a low of $148,922 in FY 1993.

The SLC has not conducted sufficient forecasting, cost-benefit, or other analyses, to determine the most effective, efficient, and economical means to meet its warehouse, distribution, and transportation needs. In recent years the SLC has ineffectively communicated to State officials its proposals to either expand the Concord warehouse or purchase one warehouse to meet SLC needs.

Ten control states and a control county own warehouses. Four other control states lease, two others lease and own, and one state does neither since a bailment operation is contracted out. Two states that own and one state that leases have contracted out the actual operation of the warehouses.

In December 1993 the SLC issued the Nashua warehouse the State's first and only liquor, wine, and beverage warehouse license. The annual license fee is $756. The Nashua warehouse has benefitted financially from its exclusive business arrangement with the State. According to a source at the Nashua warehouse, gross revenues during FY 1994 from its liquor bailment operation were expected to be approximately $2.5 million, including labor charges to the SLC, vendors, and licensees. From time to time others have wanted the opportunity to bid on the warehouse business.

RECOMMENDATION:

The SLC should assess the costs and benefits of centralizing warehouse operations and conduct an analysis of revenues and expenditures associated with owning versus leasing one warehouse. The SLC should report its findings to the Legislature by the 1996 legislative session. In the interim the SLC should request legislative authority to institute a competitive bidding process for issuing the State's one and only liquor, wine, and beverage warehouse license, as well as to award the license on a multi-year basis in recognition of any successful bidder's substantial investment.

AUDITEE RESPONSE:

The SLC concurs in part. For the complete text of the SLC's response, see Appendix D, page D-34.

OBSERVATION NO. 12: SAFETY FACTORS ACCOUNT FOR THE MAJORITY OF WORKERS' COMPENSATION CLAIMS IN THE SLC WAREHOUSE

Private sector businesses have been forced to confront worker safety issues due to federal mandates. Although State agencies are not subject to such oversight, they may realize substantial savings by instituting work-safe programs aimed at protecting employees while reducing escalating safety-related costs such as workers' compensation. As reported by an 1993 LBA performance audit on the State workers' compensation program, the SLC has been consistently one of the top five state agencies with workers' compensation liabilities. For example, in FY 1992 SLC workers' compensation expenditures were $581,000.

Warehouse employees who pick cases reported lifting approximately 800 cases daily; cases weigh 20-40 pounds on the average. Various machinery such as forklifts and motorized jacks are used to move pallets to and from the receiving and shipping dock. All warehouse personnel interviewed by the LBA expressed concerns with warehouse safety, as did the three liquor commissioners. We observed that warehouse safety procedures were insufficient and aids to reduce or prevent injuries to warehouse workers were nonexistent.

From January 1, 1990 through March 31, 1994, SLC warehouse workers' compensation claims cost the State nearly $137,000. This represented 6.9 percent of the approximately $2 million expended for warehouse employees' wages. During this period 13 employees accounted for 19 workers' compensation cases. There were, on average, 24 full-time equivalent workers employed each year. The lost time in work days was 2,087 days or the equivalent of eight person-years of work. The 19 workers' compensation cases included ten for back injuries only, two for back injury plus another area injured, and seven for other injury (non-back). Of the ten "back only" injuries, all were associated with lifting. Of the two "back injury plus other area injured," both were associated with lifting. Of the seven "other injury (non-back)," three were associated with lifting, two involved forklifts, one involved data entry, and one involved a worker getting his ankle caught between two pallets. Thus, 15 of 19 cases had injuries that were associated with lifting.

Two warehouse injuries accounted for two-thirds ($90,268) of paid workers' compensation claims during the period.

- One worker sustained a back/shoulder injury associated with lifting. A total of $45,730 was paid in workers' compensation, including an award of $25,000.

- One worker sustained an ankle injury while caught between two pallets. A total of $44,538 was paid in workers' compensation, including an award of $18,500.

3. MANAGEMENT FUNCTIONS (Continued)

3.1 MARKETING AND SALES (Continued)

OBSERVATION NO. 12: SAFETY FACTORS ACCOUNT FOR THE MAJORITY OF WORKERS' COMPENSATION CLAIMS IN THE SLC WAREHOUSE (Continued)

Safety training and safety emphasis in the warehouse were minimal. Safety procedures were insufficient and aids to reduce or prevent injuries to warehouse workers were nonexistent. Apart from a March 1994 "back clinic," warehouse workers did not participate in any training on proper lifting techniques. They also did not receive formal training on using warehouse equipment. The warehouse superintendent stated training for forklifts and other complex machinery was needed. Eight of ten warehouse personnel we interviewed reported that warehouse personnel wanted back braces. The SLC researched the feasibility of lifting belts, but due to insufficient evidence of their effectiveness refused to buy them. The SLC also has a safety committee that meets four times per year. However, the financial director questioned the productivity of the safety committee.

We observed the following unsafe conditions were allowed to exist in the warehouse that could lead to additional injuries and preventable compensation claims: (1) poor lighting, (2) poor ventilation (dust blown onto workers when heaters were cleaned), (3) unsafely stacked cases, (4) poorly maintained forklifts, (5) unsafe operation of equipment, (6) blind and unmarked corners, and (7) unauthorized smoking.

In comparison, ten of the 15 control states with warehouses (67 percent) did not report problems with workers' compensation claims. Four of the ten states require warehouse personnel to use lifting belts. Six states provide training on lifting techniques. Eight states require that personnel be trained in the use of forklift machinery. Four states require warehouse personnel be trained in the use of other machinery.

One state received a major refund from workers' compensation due to a low injury rate. Officials in this state indicated the refund was due to: (1) aggressive training programs, (2) use of lifting belts in all stores and the warehouse, (3) use of a home safety video (many injuries occur at home and are aggravated at work), (4) extensive forklift training, and (5) preventive maintenance.

Finally, all five control states experiencing problems with workers' compensation claims in the warehouse were taking action to reduce them. These actions included training on lifting techniques, safety, and machine operations. One state was re-engineering its warehouse's picking slots to reduce lifting.

3.1 MARKETING AND SALES (Continued)

OBSERVATION NO. 12: SAFETY FACTORS ACCOUNT FOR THE MAJORITY OF WORKERS' COMPENSATION CLAIMS IN THE SLC WAREHOUSE (Continued)

RECOMMENDATION:

The SLC should develop and implement a safety program for the warehouse. At a minimum this program should include safety training, preventive maintenance, and safe operations enforcement. The SLC should consult with the Bureau of Risk Management within the Department of Administrative Services regarding a safety review for the warehouse.

AUDITEE RESPONSE:

The SLC concurs in part. For the complete text of the SLC's response, see Appendix D, page D-36.

3.2 MANAGEMENT INFORMATION SYSTEMS

Sound business practices require the use of computer technology that provides necessary and reliable information to management in a useable format. As an administrative support function, management information systems should facilitate effective and efficient operations so that an organization can meet its own needs and also the needs and demands placed on it by external sources. We found several areas where MIS support should be improved.

Management information systems can provide essential support for marketing and sales functions. For example, sales forecasting is basic to marketing planning. An MIS section within a profit-generating entity such as the SLC should be capable of producing the quantitative analyses integral to such forecasts. Advertising agency personnel questioned whether the Commission's MIS operation was sufficiently sophisticated to provide the advanced support needed.

OBSERVATION NO. 13: ANALYTICAL CAPABILITIES FOR MARKETING AND SALES FUNCTION SHOULD BE IMPROVED

In-house marketing research tools for both planning and analysis were limited during the audit fieldwork. The contracted advertising agency provided most of the data regarding target markets. Sales data for evaluating marketing strategy were available in-house but did not appear to be accessible to sufficiently sophisticated PC-based analytical software for use by marketing and sales management.

3.2 MANAGEMENT INFORMATION SYSTEMS (Continued)

OBSERVATION NO. 13: ANALYTICAL CAPABILITIES FOR MARKETING AND SALES FUNCTION SHOULD BE IMPROVED (Continued)

An advertising agency-developed customer origination study conducted during FY 1994 used zip code data collected from retail customers. The study lasted one year and was reportedly to be used for future marketing planning. Data analysis was sub-contracted through the advertising budget.

Personnel from the contracted advertising agency reported needing stronger support from MIS but wondered if the system could support the types of precise analyses needed. Sales data available for evaluating marketing activities included various reports and lists dealing with variables such as dates, locations, product and size, regular and sale pricing, type of customer, weather, inventory, and gross profit. The SLC also performed rudimentary tracking of its competitors' advertising.

Data that did not appear to be readily available included discreet analyses of sales according to the type of promotion or special, the types and costs of advertising used, and pricing competition. Also absent were data regarding sales projections and performance. Sales forecasting is key to maximizing in-store product availability with minimal inventory investment.

Gross sales and profit have been increasing, albeit at a decreasing rate since FY 1992. The SLC did not have sufficient data readily available to inform short-term marketing planning or to evaluate performance of its marketing efforts. For maximum control of both the process and purpose, research on target markets and evaluation of marketing performance should be conducted in-house. Changes in advertising contractors have occurred in the past and in the future difficulties with data transfer could interrupt on-going marketing planning.

RECOMMENDATION:

The SLC should acquire software to support research in the marketing and sales function. PC-based analytical programs should be available to marketing and sales management personnel for in-house research on target markets and marketing plan performance, as well as for developing sales forecasting capability.

AUDITEE RESPONSE:

The SLC concurs in part. For the complete text of the SLC's response, see Appendix D, page D-38.

OBSERVATION NO. 14: MIS SUPPORT FOR STORES SHOULD BE IMPROVED

Management information systems within retail settings provide managers with a variety of tools to promote operational efficiency, effectiveness, and ultimately revenue production. For example, electronic mail, or E-mail, permits almost immediate transmission of information among users. Such rapid relay of information often has an added benefit of being both time- and cost-effective when compared to the slower postal mail systems. Businesses may use E-mail to swiftly exchange information and disperse essential communications, including product promotions, policy changes, and meeting notes. Another potential management information system tool for store management is store loss trend analysis. Managers act on this information to recognize and stem losses, which increases store profit and revenue production. We observed that SLC management information systems are not being used to full potential for store operations management, including the above areas.

Several store managers reported that in-store processors (ISPs) and cash registers have more capabilities than are currently used. For example, an electronic mail function had not been operationalized on ISPs. Electronic mail could be used by SLC management to transmit memoranda regarding product promotions, policy changes, and upcoming meetings. Several store supervisor/managers and managers stated they needed a minimum of one to two weeks advance notice to order inventory for store sales. However, memoranda received by store supervisor/managers and managers from the director of purchasing were not always timely. If notification was not received by stores in time to adjust the automatic product orders, sufficient product might not be delivered to that store until after the sale had started. Four store managers reported stock shortages for sales caused by insufficient notification. One supervisor/manager termed a recent wine sale a "secret sale" because "nobody" knew about it. The one to three days required to mail notification on product promotions to stores was time needed by stores to create sale tags, take down old product displays, and build new displays. Such time delays translate to revenue lost by the State.

Inventory and loss data were also underutilized by SLC management. This may be due to the data presented to management. For example, there were no trend analyses performed on store losses. Instead, various inventory control reports were used. A "swing total" report was generated and reviewed quarterly by MIS personnel. The swing total report was used by MIS personnel in conjunction with the store loss report to determine if a store had a wide variance, or "swing," in the number of bottles over and under inventory counts. The swing total report was also used to determine if product was being stolen by the bottle or the case. The MIS director reported briefing the commissioners quarterly on store losses and distributing computer reports on losses and swing totals to the commissioners and other division heads prior to the meeting. LBA auditors

3. MANAGEMENT FUNCTIONS (Continued)

3.2 MANAGEMENT INFORMATION SYSTEMS (Continued)

OBSERVATION NO. 14: MIS SUPPORT FOR STORES SHOULD BE IMPROVED (Continued)

found these reports were not self explanatory and provided little in the way of actionable data. On the other hand, if loss data were to be analyzed with pertinent store variables such as size, location, average number of employees on duty, average inventory, and sales by product then the SLC could identify trends and common factors associated with inventory losses. Perhaps those factors could be addressed by the SLC management.

On-line communications between the SLC's Concord headquarters and 68 State liquor and wine outlet stores would reduce mailing costs while increasing time efficiencies. Store managers reported they must turn on their ISPs at the start of each business day. At that time they review inventory requests and other business-related functions available through the ISP. Receiving mail and other communications at the same time would eliminate time used to travel to and from the post office, as well as eliminate unavoidable time delays in receiving mail sent from Concord.

Trend analyses of store and warehouse losses presented in summary format to commissioners and division directors could be more useful management tools and aid in the implementation of management controls.

Some MIS data may not be used to potential because the information may not be self-explanatory. The MIS director and other personnel reported there are not enough resources in the MIS Division to make the electronic mail function operational.

RECOMMENDATION:

The SLC should ensure timely notification to stores of upcoming sales and promotions. The SLC should determine whether it is feasible to continue developing an electronic mail system or to purchase software that is capable of this function. The SLC should also evaluate whether centralized adjustments may be made to store orders to accommodate upcoming sales and promotions. MIS Division personnel should develop reports that more effectively display trends in losses and problem stores. Key marketing and sales managers should consult with the MIS director to develop analytical programs related to inventory management.

AUDITEE RESPONSE:

The SLC concurs in part. For the complete text of the SLC's response, see Appendix D, page D-40.

3. MANAGEMENT FUNCTIONS (Continued)

3.2 MANAGEMENT INFORMATION SYSTEMS (Continued)

OBSERVATION NO. 15: ACCOUNTING SOFTWARE NEEDS UPGRADING

As with other areas within the SLC, significant amounts of financial management work, information and reports are integrated and generated by computer. Keeping these systems current with industry standards is critical for the SLC to develop an efficient and effective operation. However, we found that computer support for this key function was outdated.

By most standards the SLC's computerized accounting system was old, unable to provide necessary management information, and difficult to use and maintain. For example, Financial Management Division personnel reported identification numbers had to be inputted correctly or the whole number re-entered, since editing while inputting could not be done. MIS Division personnel reported there was insufficient documentation available for the system and the lack of available technical information made the system difficult to modify. MIS Division personnel stated it took "hours and hours" to fix problems and there were still instances where information was entered into the computer system incorrectly and went undetected by error checks. The MIS director stated the accounting system did not have the capabilities of many commercially-available personal computer systems, but that replacing the accounting software was not a priority in the MIS Division and probably would not occur before 1995.

Financial management personnel were often unable to provide current, accurate information. One SLC manager reported fixed assets could not be removed from the computerized fixed assets program until the end of the year because the system could not adjust properly. As a result, computerized tracking of fixed assets was not accurate until the end of the year. Additionally, information may not be generated quickly and in a format preferable to users. A list of all general ledger identification numbers in existence could not be printed with a description of their purpose. As a result, new account numbers created by supervisory personnel could not be readily verified for legitimacy by upper level management.

The SLC had been operating without technical support from the manufacturer of the accounting software for a period of about four years. The SLC's relationship with the computer software company was discontinued because a former financial management director thought the quality of user support services were not worth the expense. According to the financial director, the same software company would require the SLC to pay for fours years of software modifications prior to resuming technical support services. These computer modifications would cost the SLC $150,000.

OBSERVATION NO. 15: ACCOUNTING SOFTWARE NEEDS UPGRADING (Continued)

RECOMMENDATION:

SLC commissioners, the MIS director, and the financial management director should work together to make needed improvements to the accounting system without delay. The SLC should consult with the Office of Information Technology Management to determine the most effective means of improving the accounting system.

AUDITEE RESPONSE:

The SLC concurs. For the complete text of the SLC's response, see Appendix D, page D-42.

3.3 HUMAN RESOURCES ADMINISTRATION

Personnel management is critical for the efficient and effective management of any agency. The SLC meets the public in many ways, from its State liquor and wine outlet stores to its licensing and enforcement duties, and must ensure its personnel are knowledgeable, professional, and courteous in their dealings with the public. Areas where we observed need for improvements in human resources administration included in-service training and performance evaluations. We also observed some instances where employees were working outside of their divisions without the proper approvals.

OBSERVATION NO. 16: IN-SERVICE TRAINING IMPROVEMENTS NEEDED

As stated earlier, the SLC employs over 300 full-time classified employees and store operations alone has a part-time employee pool of 600-800 persons. Organizations train employees and maintain adequate training levels to improve organizational efficiency and effectiveness. During the audit period most SLC employees received little or no in-service training. Neither the SLC commissioners nor division heads evidenced commitment to sufficient, competent employee training. For example, the need for store employee training was widely acknowledged within the SLC from the chairman, to store operations employees, to management personnel outside the division. However, the SLC had not implemented anything to correct this obvious training deficiency.

We found the SLC had no comprehensive employee training strategy and no one to coordinate training functions. There has been no evaluation of training needs, no assessment of training opportunities, and no effort to develop meaningful in-house training programs. There has been little effort to

OBSERVATION NO. 16: IN-SERVICE TRAINING IMPROVEMENTS NEEDED (Continued)

schedule employees for training or to accurately document what little employee training actually occurred. Training records and logs were nonexistent for most SLC divisions. Only enforcement and MIS could provide any documentation. MIS training records pertained only to computer software training for SLC personnel. We have questions and concerns regarding numerous employee training inadequacies and the SLC's ability to optimize profitability, maintain proper controls assure effective and efficient operation, and provide service to customers, as required by RSA 176:3 (I-IV).

Enforcement and Regulation Division. It took several requests to obtain the enforcement training records and those we received were incomplete. We submitted preliminary observation worksheets which cited noncompliance with statutory requirements regarding minimum number of training hours and content for liquor investigators, as well as for certifying to the Police Standards and Training Council that those requirements had been met. Subsequently, enforcement personnel found some of the missing training records and made them available to us.

The Enforcement and Regulation Division could not provide course outlines and attendance rosters for much of the in-house training held from 1989-1992. All outlines received and ten of the 12 attendance rosters submitted by enforcement needed improvement. Deficiencies included outlines not clearly describing topics, not specifying the total hours of training received, or the amount of time spent on each topic. Further, rosters sometimes appeared to be an afterthought. Names of investigators who attended training were often handwritten on outlines, "all" was scribbled on the outline, or just employee signatures were present.

Finally, the enforcement and regulation chief submitted in-service compliance reports to the Police Standards and Training Council attesting that all investigators had completed eight hours of training annually from 1989-1992. However, the division could not provide us with sufficient documentation to substantiate that all liquor investigators had completed eight hours of in-service training in each year in accordance with RSA 188-F:27 (VII) and Pol 403.01.

The SLC, by submitting signed compliance reports, misinformed the Police Standards and Training Council regarding its compliance with State training and documentation requirements. According to the director of the Police Standards and Training Council, the enforcement and regulation chief could be suspended or his police officer certification revoked for not taking adequate steps to ensure and document that liquor investigators meet State training requirements.

OBSERVATION NO. 16: IN-SERVICE TRAINING IMPROVEMENTS NEEDED (Continued)

Store Operations. We found a significant need for more training in store operations. This need was widely acknowledged within the SLC by everyone from the chairman, to store operations employees, to management personnel outside the division.

Store operations management reported that training should be increased and improved for all staff, especially part-time employees. Management personnel reported inadequate training regarding product knowledge, in-store computers, customer service, and liability areas such as sales to minors and inebriates.

SLC managers outside of store operations also reported training needs for store personnel. Marketing and Merchandising Division management reported that store management and employees have insufficient knowledge of wines. (The wine marketing specialist trained only personnel in the three original premium wine stores. During FY 1994, there were 21 such locations.)

Lack of training in wines means some SLC store managers do not order premium wines that are in demand. The SLC may be losing sales due to this unmet customer demand. Improperly trained and uninformed employees also are unable to answer customers' questions and may provide incorrect information to customers. Knowledgeable staff are often diverted from other duties in order to provide customer service. Employees who are ill-prepared detract from the shopping experience and may increase SLC liability due to sales to underage or intoxicated individuals. (One store manager stated that lack of ID training by store personnel resulted in sales to underage customers, as evidenced in a recent "sting operation.")

In the mid-to-late 1980s, the SLC conducted a comprehensive training program in collaboration with the UNH Division of Continuing Education and the Whittemore School of Business. The program, which cost approximately $100,000 annually, lapsed in 1990 due to budget reductions. Store personnel reported the UNH/SLC program trained approximately 30 personnel from all levels of the Store Operations Division. These 30 personnel in turn trained up to 90 percent of the store division's remaining personnel. Employees received half-day training sessions.

Our review of the UNH program indicated the training modules were comprehensive and appropriate for enhancing efficient and effective store operations. Personnel who received the training stated it helped resolve store problems and built confidence. One store manager commented that this "train the trainer" program was the best training the stores ever had and should be reinstated. (This manager still used a training checklist developed by the program.)

OBSERVATION NO. 16: IN-SERVICE TRAINING IMPROVEMENTS NEEDED (Continued)

Financial Management. Financial management employees have not received sufficient training and cross-training. MIS Division personnel who maintain the accounting system reported some financial management personnel did not have sufficient knowledge to operate the system. A unit supervisor was not taught pertinent administrative rules and State laws affecting daily job activities by the former supervisor. The division director stated he had incorrectly assumed the former supervisor had properly trained the new supervisor and later discovered that was not true.

The financial management director has not made training a priority. All of the supervisory accounting personnel we interviewed stated training, especially cross-training, needed to be improved. They identified training on basic accounting, updates on new accounting procedures, and computer review courses as needed.

Cross-training ensures that more than one person knows how to complete the work of other employees who are unavailable due to vacation, sickness, or termination. We identified three functions important to division operations where employees were not cross-trained. The first function was oversight of daily operations in the accounts payable, accounts receivable, general ledger, and payroll units. The second function was reviewing and processing all SLC bills except those pertaining to liquor and freight. The third function involved credit card processing.

Training for MIS personnel has been sporadic. Training declined significantly after 1990 and was limited to seminars or computer trade shows. In addition, the human resources administrator stated that most SLC training is now on-the-job training and that there is a definite need for training within all divisions.

Training promotes maintenance and improvement in employee skills. It enables personnel to assimilate and master new skills. Properly trained and informed employees are able to answer questions from the public, efficiently perform their jobs, and promote agency goals. Without adequate training knowledgeable staff may be diverted from their duties to assist employees who lack necessary skills and training. Without adequate training the SLC's ability to optimize profitability, maintain proper controls, assure effective and efficient operation, and provide service to customers, as required by RSA 176:3(I-IV), is jeopardized.

OBSERVATION NO. 16: IN-SERVICE TRAINING IMPROVEMENTS NEEDED (Continued)

According to the National Commission on the State and Local Public Service "a high-performance work force requires a well-executed training program." The commission recommends the creation of "a learning government by restoring employee training and education budgets."

RECOMMENDATION:

The SLC should evaluate training needs and implement adequate training programs for employees in all SLC divisions. A training coordinator position should be established within existing resources to facilitate this process, to identify existing training resources within the SLC and other State agencies, and to maintain centralized training records.

The SLC should develop and implement a comprehensive training program for all store employees including part-time and temporary personnel.

Training records from 1989-1992 for the Enforcement and Regulation Division should be brought up to standard with outlines and attendance rosters as required by administrative rule Pol 403.01. At a minimum, training documentation should include: content, length, relevance, and frequency of all course offerings, as well as the year the course was credited towards an investigator's in-service requirement. When multiple topics are covered in training, the time break down for each segment should be noted, as well as which segments do or do not count towards in-service requirements. Attendance rosters should be in the form of sign-in sheets with the typed name of the employee and the signature of the employee next to the typed name. Backup copies of all training information submitted to the Police Standards and Training Council should be retained at the SLC central office.

The SLC should request the Police Standards and Training Council audit the Enforcement and Regulation Division for compliance with State training and documentation requirements. In the future the SLC should ensure that adequate oversight of in-service training and compliance with training and documentation requirements occurs.

Financial management personnel should maintain technical and professional proficiency through continual training and cross-training. Regular access to training should be recommended by senior personnel to ensure the division's needs are being addressed. Financial management personnel should be trained and cross-trained within accounting units to ensure duties are fulfilled even when an employee is absent from the office.

AUDITEE RESPONSE:

The SLC concurs in part. For the complete text of the SLC's response, see Appendix D, page D-43.

3. MANAGEMENT FUNCTIONS (Continued)

3.3 HUMAN RESOURCES ADMINISTRATION (Continued)

OBSERVATION NO. 17: SLC EMPLOYEES NOT EVALUATED ANNUALLY AS REQUIRED

RSA 21-I:42 (XIII) and administrative rule Per 801.06 requires all full-time classified employees to receive written performance evaluations at least annually. Performance evaluations are required before employees receive annual increments according to Per 901.03. The SLC employed approximately 305 full-time employees during FY 1994. Interviews with personnel at various levels within several divisions indicated performance evaluations were not being conducted in compliance with State requirements. A review of personnel records indicated this situation was typical throughout the SLC. On average, SLC employees receive personnel evaluations approximately every 3.5 years. One employee had no record of receiving an evaluation for more than 25 years.

Performance evaluations are not stressed by the commissioners. One commissioner stated that it was "about time" the commissioners performed evaluations of some division directors. A second commissioner could not affirm the existence of a formal evaluation system, nor did the commissioner know if evaluations were done yearly.

SLC personnel reported that the human resources administrator tracked when performance evaluations were due and notified supervisors. Such notification was routinely ignored. SLC supervisors stated the following reasons for not conducting employees' performance evaluations: (1) "The last stores director never pressed us to do performance evaluations because he never did them;" (2) "due to moving to a different part of the state, I only did some evaluations;" (3) "I'm not big on performance review we have here; don't care for the format;" and (4) evaluations not given because supervisor didn't know employees' jobs.

The SLC did not administer timely evaluations and consequently employees were denied their right to participate in annual evaluations. The SLC failed to use an important management tool. Performance evaluations are key providers of communication and feedback to employees. Evaluations provide employees with specific written performance expectations and criteria and detail employee strengths and weaknesses. They critically document employee excellence, average performance, or sub-par achievement.

Lack of evaluations affects employee morale and efficiency. Excellent employees may be unrewarded or unacknowledged. Other employees are not informed of the criteria for improved performance.

RECOMMENDATION:

The SLC should require all full-time classified employees receive written performance evaluations at least annually, in accordance with RSA 21-I:42 (XIII) and administrative rule Per 801.06.

OBSERVATION NO. 17: SLC EMPLOYEES NOT EVALUATED ANNUALLY AS REQUIRED (Continued)

AUDITEE RESPONSE:

The SLC concurs. For the complete text of the SLC's response, see Appendix D, page D-51.

OBSERVATION NO. 18: EMPLOYEES WORKING OUTSIDE OF OWN DIVISION WITHOUT DIVISION OF PERSONNEL APPROVAL

Human resources management is responsible for coordinating and monitoring personnel management programs and resolving staffing problems. In addition, the SLC's human resources administrator is responsible for ensuring Commission compliance with Division of Personnel administrative rules. These rules are specific regarding intra-agency transfer, position reclassification, and other areas. Our analysis indicated the SLC reassigned three employees to different responsibilities without complying with Division of Personnel administrative rules. The SLC human resource administrator reported being unaware of Division of Personnel requirements regarding reassignments.

First, a Word Processor Operator II was being paid from Financial Management Division appropriations but had been completing MIS Division administrative tasks and acting as a software trainer for the SLC since 1991. In April 1993, commissioners formally approved a request to transfer this employee into the MIS Division. The Financial Management Division director verbally informed the administrative assistant in June 1993 that the commissioners had rescinded the transfer request. When asked, SLC management could not provide documentation regarding when or why this transfer was rescinded. However, the majority of work done by the administrative assistant continued to be for MIS not financial management.

Second, a store supervisor/manager worked for the MIS Division but his salary continued to be paid by the Store Operations Division. This store supervisor/manager had been completing assignments related to the shelf management program being developed by MIS and other miscellaneous tasks since June 1992. The MIS director stated this supervisor/manager worked full-time collecting data for shelf management and doing low-level programming. The SLC's human resource administrator stated the reassignment of this supervisor/manager was temporary.

OBSERVATION NO. 18: EMPLOYEES WORKING OUTSIDE OF OWN DIVISION WITHOUT DIVISION OF PERSONNEL APPROVAL (Continued)

Third, a store supervisor/manager had been transferred to the SLC Concord office as the assistant to the Store Operations Division director. This reassignment took place in September 1990. According to the supervisor/manager, the reassignment was to be on a temporary basis. The supervisor/manager stated he did not interview for this job. Technically his job title was still supervisor/manager, and he was compensated as a supervisor/manager. According to the SLC human resources administrator, the SLC did not seek or receive approval by the director of the Division of Personnel regarding the reassignment of this supervisor/manager. The human resource administrator stated this supervisor/manager's supplemental job description was in the process of being revised to reflect current responsibilities. The supervisor/manager also stated he intended to apply for an upgrade to increase his compensation level.

If the SLC intended to temporarily reallocate or reclassify all three employees, it should have proceeded by formally requesting to do so in accordance with Per 303.07 (a)(b)(c). Administrative rule Per 303.07 (a)(b)(c) allows agencies to request temporary reallocation or reclassification of positions when more than ten percent of total working time has been delegated to the position, specifies documentation requirements of State agencies to provide to the Division of Personnel, but limits temporary reallocation or reclassification of positions to six months. We found that all three of these employees were reallocated to different positions for more than six months.

If the SLC intended to temporarily appoint the two supervisor/managers to other positions within the SLC, it should have applied to do so in accordance with Per 601.01 (c). According to this rule, temporary appointments may be made only to temporary positions classified by the Division of Personnel, and a temporary appointment can be no longer than one year in duration. The SLC has exceeded the one year temporary appointment limit for these two supervisor/managers since these employees have been in new positions for two or more years. Further, the SLC had not complied with Per 301.05 (a)(7). Per 301.05 (a)(7) considers reassignments to positions for longer than 12 months to be new positions and requires agencies to obtain approval from Governor and Council.

If the SLC intended to transfer the one supervisor/manager and word processor operator II to the MIS Division, it should have requested approval from the director of the Division of Personnel pursuant to Per 302.02. Administrative rule Per 302.02 (a) prohibits permanent transfers of positions from any other department subdivision to another without the

OBSERVATION NO. 18: EMPLOYEES WORKING OUTSIDE OF OWN DIVISION WITHOUT DIVISION OF PERSONNEL APPROVAL (Continued)

review and approval of the director of personnel. Subdivision (b) of Per 302.02 requires the director of personnel receive and review written documentation regarding the positions affected by the proposed transfer or assignment, as well as, the reasons for the change, before the change is made.

The SLC has not complied with Division of Personnel administrative rules. The temporary assignments of supervisor/managers to positions within the SLC main office created additional responsibilities for other supervisor/managers. Responsibilities for stores previously under the supervisor/manager working in the MIS Division were transferred to two other supervisor/managers.

According to a commissioner these two supervisor/managers were "overloaded." SLC supervisor/managers affected by this situation stated they were not able to complete all tasks required due to their additional responsibilities. Finally, the SLC in effect transferred appropriated funds between divisions to pay for the administrative assistant's and one supervisor/manager's salaries without proper approvals.

RECOMMENDATION:

The SLC should reassign the two supervisor/managers to their positions within the Store Operations Division. The word processor operator II position should be reviewed and a determination made as to whether the position should be reallocated and transferred to the MIS Division. The SLC should follow procedures required by the Division of Personnel administrative rules for transfer or reassignment of positions to different divisions. The human resources administrator should familiarize himself with pertinent administrative rules to effectively respond to future inquiries by SLC managers and employees.

AUDITEE RESPONSE:

The SLC concurs in part. For the complete text of the SLC's response, see Appendix D, page D-52.

3.4 ENFORCEMENT AND REGULATION

We observed two areas where improvements in the licensing and enforcement area would enhance efficiency and effectiveness. These include changing the renewal cycle for liquor licenses and providing additional support for liquor investigators.

OBSERVATION NO. 19: SLC SHOULD ANALYZE THE EFFECTIVENESS OF A TWO-YEAR RENEWAL CYCLE FOR MOST LIQUOR LICENSES

The Enforcement and Regulation Division is responsible for issuing annual liquor licenses and enforcing State liquor laws. The division reported there were approximately 3,500 licenses in FY 1993. Division management reported a shortage of investigators, and we are concerned that yearly licensing requirements are an inefficient use of limited investigative staff.

SLC investigators spend up to 60 percent of their time processing license applications and renewals. In addition, RSA-179:57 (I) requires frequent inspections of licensee premises. Investigators report making inspections anywhere from once a month to twice a year. The more time spent processing licenses and renewals, the less time spent conducting investigations.

RECOMMENDATION:

The SLC should analyze the efficiency and effectiveness of establishing a two-year renewal cycle for licenses. Issues that should be included in this analysis include the following: (1) the procedures and functions required for issuing and renewing licenses, (2) the percent of investigator workload solely devoted to issuing and renewing licenses, and (3) the impact of the licensing requirement on other statutory requirements for investigative personnel such as inspections, investigations, and education. If the outcome of the analysis warrants, the SLC should request the Legislature amend RSA 178:27 (I-V,VII-VIII) to change the liquor license renewal cycle from one year to two years.

AUDITEE RESPONSE:

The SLC concurs. For the complete text of the SLC's response, see Appendix D, page D-54.

OBSERVATION NO. 20: MATERIAL SUPPORT FOR HOME OFFICES OF LIQUOR INVESTIGATORS SHOULD BE INCREASED

Each Enforcement and Regulation Division liquor investigator maintains an office in his or her home. Weekly office hours are 8:00 - 10:00 a.m. four days per week. The investigators use their home telephones to conduct State business. Investigators' home telephone numbers are published in liquor law books distributed to licensees and to the public. The SLC does not pay for the telephone lines, but does pay for long distance telephone calls via credit card.

Investigators reported that they and family members frequently receive calls outside of office hours. Four investigators stated that some calls were threatening. The division chief remarked that calls affecting family members were increasing. Individuals have shown up uninvited at investigators' houses and harassed investigators and their families.

Other State law enforcement agencies including the Division of Safety Services, the Fish and Game Department and the State Police do not require their personnel to have personal home telephone numbers published.

Investigators must furnish their home offices with necessary equipment such as a desk, file cabinets, a typewriter, or a computer. The division's central office has some supplies available for investigators such as paper clips, pens, pencils, and paper. All investigators may use the central office photocopier. According to the administrative assistant chief, this photocopier is used by investigators in proximity to the central office. The administrative assistant chief also stated that some investigators located away from the central office have informal agreements to use photocopiers at nearby police departments.

RECOMMENDATION:

The SLC should provide in-home office telephone lines to investigators who request them for SLC business-related calls. For public convenience telephone answering machines should also be supplied for incoming calls after office hours. The SLC should also consider providing post office boxes for investigators. Finally, the SLC should reimburse investigators for all necessary out-of-pocket expenditures.

AUDITEE RESPONSE:

The SLC concurs in part. For the complete text of the SLC's response, see Appendix D, page D-56.

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STATE OF NEW HAMPSHIRE
STATE LIQUOR COMMISSION

MANAGEMENT CONTROLS

4. MANAGEMENT CONTROLS

Effective management controls are essential to achieving the proper conduct of government business with full accountability for the resources made available. Controls facilitate the achievement of management objectives by serving as checks and balances against undesired actions. Controls are also intended to ensure that reliable data are obtained, maintained, and fairly disclosed in reports and that the agency complies with laws and regulations.

Management controls consist of an agency's methods, policies, and procedures for defining the internal work processes of the agency, for meeting its operational goals and objectives, and for ensuring compliance with State laws and other regulations.

Because of the diffuse organizational structure we observed at the SLC, we expected to find specific policies and procedures for each division, as well as general ones which covered activities pertinent to the entire agency. Instead, we found detailed and up-to-date policies and procedures only in enforcement and regulation. In some divisions, financial management for instance, we initially encountered resistance to the concept of written policies and procedures. This changed during the course of the audit, to the point where one functional supervisor was assigned responsibility for writing policies and procedures for the accounting functions.

We assessed SLC management controls to determine whether controls were timely, consistently applied, documented, and supported by management. We determined the SLC's management control structure needed improvements to ensure efficient operations and to minimize the potential for possible fraud and possible abuse. We reviewed possibly fraudulent actions concerning the advertising contract, personnel actions, and State purchasing rules, as well as possible abuse in the form of preferential treatment of a New Hampshire-based liquor manufacturer. We also observed numerous control problems within the administrative support functions that concern accounting and MIS. Store operations should update its policies and procedures and review security procedures in the retail locations, while warehouse operations needed additional controls for inventory and security. Improvements in file security and documentation of significant processes are needed in enforcement and regulation. Additional administrative rules should be promulgated in three areas, while some advertising practices may be out of compliance with State and federal laws.

4. MANAGEMENT CONTROLS (Continued)

4.1 QUESTIONABLE ACTIONS

During the course of the audit we became aware of several situations which we considered to be highly irregular and in some cases potentially fraudulent. Based upon our discussions with the commissioners and other SLC personnel, we contacted the attorney general with our concerns. Several of our findings pertain to questionable use of advertising contract funds (Observation Nos. 21-25), including a software development sub-contract that was awarded to an SLC employee. Other questionable actions included equipment purchases (Observation No. 26), personnel violations (Observation Nos. 27 and 28), and preferential treatment of a liquor manufacturer (Observation No. 29).

OBSERVATION NO. 21: ADVERTISING CONTRACT USED FOR NON-ADVERTISING PURPOSES

From FY 1992 through FY 1994 nearly $39,000 in funds appropriated specifically for advertising were shifted to other uses by the SLC without the approval of Governor and Council. First, during FY 1992 the SLC authorized the diversion of $30,000 from the advertising contract appropriation to develop a shelf management program. Second, in fiscal years 1992, 1993, and 1994, the SLC expended $8,972 in funds from the advertising contract to pay for production, contest award dinners, and prizes for store employees. This program, called the "Golden Knife Award," is open only to store employees and awards prizes for store displays set up during the holiday season.

The liquor commissioners identified the shelf management program as a priority. However, according to the SLC chairman advertising funds were used because other priorities "didn't leave sufficient resources to do shelf management until some point in the future." The SLC chairman further stated that money for the shelf management program was specifically appropriated in the advertising agency budget. The liquor commissioners stated the advertising contract was used for the Golden Knife contest awards because the contest was an advertising and merchandising activity, was designed to initiate employee motivation through techniques for merchandising, and was a point of sale activity included in the advertising contract.

Advertising agency personnel responsible for the SLC contract stated that at the beginning of the FY 1992 contract term, they were instructed by the commissioners to budget $50,000 for shelf management. These personnel stated further that they did not know what shelf management was, but it was outside of their area of expertise. They also stated that shelf management was related to merchandising, but not advertising. Likewise, advertising personnel have described the Golden Knife Award's contest, awards dinner, and prizes as being "very important for merchandising; not advertising but it is promotion."

4. MANAGEMENT CONTROLS (Continued)

4.1 QUESTIONABLE ACTIONS (Continued)

OBSERVATION NO. 21: ADVERTISING CONTRACT USED FOR NON-ADVERTISING PURPOSES (Continued)

We reviewed budget-related documents from FY 1992 including the operating budget, the statement of appropriation, the advertising budget submission documents from the SLC, and the SLC advertising contract, but could not find any reference to either shelf management or the Golden Knife Award.

RSA 9:19 states: "No state official, commissioner, trustee, or other person having control of public funds appropriated by the general court shall use any part of such funds for any other purpose than that for which they were appropriated...."

RECOMMENDATION:

We recommend the attorney general investigate to determine whether the SLC commissioners have violated the provisions of RSA 9:19.

AUDITEE RESPONSE:

The SLC does not concur. For the complete text of the SLC's response, see Appendix D, page D-58.

For attorney general response, see Appendix E.

OBSERVATION NO. 22: NO-BID CONTRACT INAPPROPRIATELY AWARDED TO MIS DIRECTOR

The SLC did not comply with State laws in awarding a $30,000 software development contract to one of its own employees. The contract was awarded without competitive bidding and without Governor and Council approval.

In April 1992, the SLC chairman directed the commission's advertising contractor to bill the SLC for $30,000 and to employ a sub-contractor to develop a shelf management system. Two months later, the commission again directed the contractor to invoice the SLC $30,000 and contract with the commission's MIS director to develop a computerized shelf management system.

RSA 4:15 requires the expenditure of any funds appropriated to any department to be subject to the approval of Governor and Council. The June 1992 letter authorizing the contract with the MIS director states the SLC conducted "appropriate review," as well as "consultation with the attorney general's Office" and "discussions with several members of the Executive Council." We contacted the attorney general and were informed by the senior assistant attorney general handling SLC matters at the time that he could not recall approving the arrangement. We also found no record of Governor and Council approval.

OBSERVATION NO. 22: NO-BID CONTRACT INAPPROPRIATELY AWARDED TO MIS DIRECTOR (Continued)

RSA 21-I:11 (III) requires competitive bidding before making any purchase for the State except when the expenditure is not more than $2,000, when reasonable investigation indicates the unit or item is procurable from only one source or the unit or item has a fixed market price, or when in the Governor's opinion an emergency exists requiring immediate procurement. In addition, RSA 21-I:11 (XI) requires an agency to obtain approval for procurement from the director of the Office of Information Technology Management before submitting a Request For Proposal for State data processing equipment, software, or services exceeding $5,000 in total cost. RSA 21-I:11 (XII) requires agencies to submit the approval from the Office of Information Technology Management in support of requests for purchases, equipment, or software in excess of $5,000. None of the provisions of RSA 21-I:11 were followed.

The contract with the MIS director was awarded on a sole-source basis, and documentation provided by the SLC justifying such a decision was insufficient. The documentation consisted of a one-page "initial evaluation" of two commercially-available shelf management programs and was dated five weeks after the contract was authorized and awarded.

RECOMMENDATION:

We recommend the attorney general investigate to determine whether the SLC commissioners have violated the provisions of RSAs 4:15 and 21-I:11.

AUDITEE RESPONSE:

The SLC does not concur. For the complete text of the SLC's response, see Appendix D, page D-61.

For attorney general response, see Appendix E.

OBSERVATION NO. 23: CONFLICT OF INTEREST FOR MIS DIRECTOR IN ACCEPTING SHELF MANAGEMENT CONTRACT

The SLC's MIS director was awarded a $30,000 contract to develop an information system that was within the purview of his official duties and responsibilities. The MIS director performed an evaluation of commercially-available shelf management packages and submitted it to the SLC. The submission date of this evaluation was July 29, 1992. This was five weeks after the SLC had directed its advertising contractor to award the contract to develop the shelf management program to its MIS director.

4. MANAGEMENT CONTROLS (Continued)

4.1 QUESTIONABLE ACTIONS (Continued)

OBSERVATION NO. 23: CONFLICT OF INTEREST FOR MIS DIRECTOR IN ACCEPTING SHELF MANAGEMENT CONTRACT (Continued)

The MIS director's job description requires that he be responsible for acquisition, planning, and design for all information systems and data processing. The MIS director reported that the SLC said shelf management was a priority and critical, and that he told the commissioners he would get it done in 12 months. However, as of February 1995, the shelf management system had not been implemented. The MIS director also reported to us that "nobody in the MIS division had the mathematical and technical knowledge to do the code" and that he "was not hired to be a programmer here and was not going to do it for free."

RSA 95:1 prohibits any public employee from contracting, except in open competitive bidding, to sell goods or personal property to the State or political subdivision under which the employee holds public office. A 1987 attorney general's opinion (No. 1987-30) clearly supported the statute's applicability to State employees.

RECOMMENDATION:

We recommend the attorney general investigate to determine whether the SLC commissioners or the MIS director have violated provisions of RSA 95:1.

AUDITEE RESPONSE:

The SLC does not concur. For the complete text of the SLC's response, see Appendix D, page D-61.

For attorney general response, see Appendix E.

OBSERVATION NO. 24: OWNERSHIP OF INTELLECTUAL PROPERTY IN QUESTION

The SLC issued a contract to its own MIS director to develop computer software for its use. No formal agreement was written and signed by all the parties to the contract, but the sum of $23,569 ($20,475 labor, $3,094 equipment) was billed by the MIS director and authorized for payment by the SLC chairman. Each invoice contained statements indicating: (1) the MIS director retained unlimited patent, trademark, and commercial rights to the program; (2) the MIS director would provide the SLC with a copy of each program in source and executable form, as well as all relevant data and documentation; (3) the SLC would receive unrestricted and perpetual right to use the program internally; and (4) the program would not be accessible to third parties. Apart from the questionable legality of the contract and the process for awarding it (discussed in other observations), these terms may be excessively disadvantageous to the SLC.

4. MANAGEMENT CONTROLS (Continued)

4.1 QUESTIONABLE ACTIONS (Continued)

OBSERVATION NO. 24: OWNERSHIP OF INTELLECTUAL PROPERTY IN QUESTION (Continued)

First, the SLC may have inappropriately granted ownership to potentially marketable software. Commercially-available shelf management programs typically sell for $40,000-$50,000. Second, the SLC may have unnecessarily restricted its own future access to the program by agreeing to not make the program accessible to third parties. If the MIS director were to leave SLC employment, the SLC might be precluded from hiring an outside source to maintain the program.

RECOMMENDATION:

We recommend the attorney general investigate to clarify ownership and other rights to the shelf management program.

AUDITEE RESPONSE:

The SLC concurs. For the complete text of the SLC's response, see Appendix D, page D-65.

For attorney general response, see Appendix E.

OBSERVATION NO. 25: BREACH OF ADVERTISING CONTRACT TERMS AND CONDITIONS

Although the contract between the SLC and its advertising contractor for the period FY 1992 through FY 1995 contains conflicting provisions (the contract contains both current and former boilerplate language relating to general terms and conditions typically included in all State contracts), a reasonable interpretation of either leads to the conclusion that the award of a $30,000 subcontract to the SLC's MIS director, a State employee, to develop a computerized shelf management program was specifically prohibited.

Section 6.2 of the boilerplate currently used by State agencies prohibits the contractor from subcontracting with a State employee. Section 8.2 of the boilerplate formerly used by State agencies prohibits the contractor from subcontracting with a State employee without the written approval of the State (section 21 also requires such approval be authorized by Governor and Council). Additionally, section 14 of the former boilerplate, relating to conflict of interest, stipulates that no State employee who reviews or approves any of the services under the contract, "Shall participate in any decision relating to this agreement which affects his or her personal or pecuniary interest...."

OBSERVATION NO. 25: BREACH OF ADVERTISING CONTRACT TERMS AND CONDITIONS (Continued)

RECOMMENDATION:

We recommend the attorney general investigate to determine whether directing the advertising contractor to award a subcontract to the SLC's MIS director violated any of the terms and conditions of the SLC advertising contract.

AUDITEE RESPONSE:

The SLC does not concur. For the complete text of the SLC's response, see Appendix D, page D-61.

For attorney general response, see Appendix E.

OBSERVATION NO. 26: NONCOMPLIANCE WITH STATE PURCHASING REQUIREMENTS

The SLC has not complied with State purchasing statutes and rules. On four separate occasions during 1992 and 1993 the SLC did not use competitive bidding as required by RSA 21-I:11 (III) to purchase goods and services which cost more than $2,000. The SLC did not provide any evidence documenting it had conducted a reasonable investigation determining the goods and services were only available from one source. Further, none of these SLC purchases were exempt from purchasing requirements governing the procurement of goods and services under RSA 21-I:18 (I)(b) which exempts the SLC from purchasing requirements for liquor and insurance, as well as leasing and equipping its stores, warehouse, and other merchandising facilities for the sale of liquor.

In 1992 and 1993 the SLC had three different vendors submit separate consecutive "repair" invoices in amounts of $1,000 or less, when actually services or equipment had been purchased. The SLC purchased: 1) new woodworking equipment totaling $2,876.50, 2) new second floor office windows totaling $7,900 including installation, and 3) new first floor carpeting totaling $4,322 including installation. The SLC also paid for computer training totaling $3,640 by having the vendor submit separate invoices for training services in amounts under $1,000. In March 1994 we reviewed the SLC's equipment inventory of fixed assets but equipment purchases noted above were not listed because the equipment had been billed as repairs. In June 1994 the SLC provided auditors with a fixed assets additions list which included the woodworking equipment and office windows. An explanation was on the list stating the items were purchased in FY 1993 but capitalized in FY 1994. SLC personnel reported the items were added to the fixed assets inventory in light of discussions with LBA auditors.

OBSERVATION NO. 26: NONCOMPLIANCE WITH STATE PURCHASING REQUIREMENTS (Continued)

According to RSA 9:16-a, a department may transfer funds among all program appropriation units (PAUs) within the department if prior approval by the Fiscal Committee and Governor and Council has been obtained. In effect, the SLC transferred funds among PAUs to pay for woodworking equipment without first obtaining necessary Fiscal Committee and Governor and Council approvals. The SLC paid for the woodworking equipment from the Office of the Commissioners as maintenance other than buildings and grounds, instead of the Store Operations Division as equipment.

Goods and services acquired by the SLC are subject to State purchasing rules and pertinent statutes. By not following purchasing requirements, the State had no control over which vendors were selected, whether fees charged were efficient and appropriate, and whether the services received were appropriate to the circumstances and needs of the SLC. Further, building improvements and equipment did not exist according to State fixed asset records, were not tracked for inventory purposes, nor depreciated accordingly until one year after purchase. The building improvement that resulted with the installation of new carpeting is still not documented in State fixed asset records.

RECOMMENDATION:

We recommend the attorney general investigate whether the SLC violated the provisions of RSA 21-I:11. We further recommend the SLC develop and implement written policies and procedures regarding procurement of goods and services in accordance with State purchasing requirements, as well as provisions on management controls and supervisory review.

AUDITEE RESPONSE:

The SLC concurs. For the complete text of the SLC's response, see Appendix D, page D-67.

For attorney general response, see Appendix E.

OBSERVATION NO. 27: NONCOMPLIANCE WITH STATE LAWS REGARDING TEMPORARY AND PART-TIME EMPLOYEES

Beginning on April 1, 1993, the SLC allowed a part-time employee in one of its liquor outlet stores to consistently work 40-hour work weeks. On July 1, 1993, the employee began to receive medical and dental benefits at the State's expense. The employee continued working 40-hour weeks and receiving State benefits through March 1994. The total cost of the medical and dental

OBSERVATION NO. 27: NONCOMPLIANCE WITH STATE LAWS REGARDING TEMPORARY AND PART-TIME EMPLOYEES (Continued)

insurance premiums paid by the State amounted to $3,832. We have not determined the cost to the insurer of benefits received by the part-time employee.

RSA 98-A:6-a (Health and Dental Benefits) requires permanent part-time employment of more than 30 hours per week, and for a duration of six months or more, before a part-time employee is entitled to elect to receive the health and dental insurance benefits afforded full-time State employees. In addition, the employment must be approved by the State Division of Personnel. As part of its process, the division verifies with the Department of Administrative Services budget office that the agency has sufficient funds budgeted for the employee's salary and benefits. The part-time employee was not approved by the State Division of Personnel to work over 30 hours per week, nor was the SLC given approval by the division to pay the employee's medical and dental insurance premiums.

SLC and State Division of Personnel officials and employees told us that liquor commissioners had personally interceded on the employee's behalf. The part-time employee's spouse is an officer of a State political party organization and reportedly works for a former high-ranking State official. SLC personnel and the director of the State Division of Personnel reported the spouse had a major illness. In addition, the SLC chairman indicated in a hand written note that at least one member of a current high-ranking State official's staff would also intercede on behalf of the part-time employee. The State director of personnel reported personally informing a SLC commissioner at the beginning of February 1994 that the employment was illegal and that the employee had to be returned to part-time service. However, the situation was allowed to continue through the end of March 1994.

Chapter 261:1, Laws of 1990 (House Bill 1506), requires agencies with open full-time positions to hire the first qualified person previously laid off from State service. If there are no qualified employees laid off from the agency, then the next qualified person laid off from any other State agency between January 1, 1990 and December 1, 1990 must be given the available position.

State law was not followed by the SLC regarding the full-time employment of the part-time employee. A part-time employee was given favorable treatment, allowed to work full-time hours, and given health and dental benefits. State expenditures for medical and dental insurance premiums were inappropriately incurred. One or more liquor commissioners may have allowed the SLC to be susceptible to outside political influence.

OBSERVATION NO. 27: NONCOMPLIANCE WITH STATE LAWS REGARDING TEMPORARY AND PART-TIME EMPLOYEES (Continued)

RECOMMENDATION:

We recommend the attorney general investigate to determine whether any SLC commissioners have violated provisions of RSA 98-A:6-a or other applicable laws. We further recommend pursuant to RSA 9:19 and RSA 9:20 the SLC seek reimbursement for health and dental insurance premiums wrongfully paid in the amount of $3,832.

AUDITEE RESPONSE:

The SLC concurs in part. For the complete text of the SLC's response, see Appendix D, page D-68.

For attorney general response, see Appendix E.

OBSERVATION NO. 28: ABUSE OF STATE LAWS REGARDING APPOINTMENTS TO THE CLASSIFIED STATE SERVICE BY LIQUOR COMMISSIONERS

As noted above, between April 1993 and March 1994 the SLC allowed a part-time employee in one of its liquor outlet stores to work 40-hour work weeks. This is in violation of State law and personnel rules. At least one and perhaps two liquor commissioners personally interceded on the employee's behalf to maintain the employee's 40-hour status. The part-time employee's spouse is an officer of a State political organization.

One liquor commissioner was reported to be actively attempting to create a permanent full-time position for the part-time employee. This full-time position would have involved transferring positions between stores so the employee could remain in a 40-hour position at the same store. Evidence was found on an internal SLC memorandum, referring to possible actions on behalf of the part-time employee by a member of a current high-ranking State official's staff.

RSA 21-I:52 (I) prohibits any person from using any official authority or influence to secure or attempt to secure for any person an appointment or an advantage in appointment to a position in the classified service for any political or other consideration.

OBSERVATION NO. 28: ABUSE OF STATE LAWS REGARDING APPOINTMENTS TO THE CLASSIFIED STATE SERVICE BY LIQUOR COMMISSIONERS (Continued)

RECOMMENDATION:

We recommend the attorney general investigate to determine whether any SLC commissioners violated the provisions of RSA 21-I:52 (I).

AUDITEE RESPONSE:

The SLC concurs in part. For the complete text of the SLC's response, see Appendix D, page D-68.

For attorney general response, see Appendix E.

OBSERVATION NO 29: PREFERENTIAL TREATMENT OF LOCAL LIQUOR MANUFACTURER

SLC commissioners, division heads, and other personnel acknowledged that the only New Hampshire-based liquor manufacturer has not been billed and therefore has not paid Concord warehouse charges for bailment, shipping, and handling. We determined that from March 1992 through February 1994 the local manufacturer has incurred but not paid the SLC $345,780.98 in bailment and other warehouse charges. From April 1992 through February 1994, the local manufacturer consistently ranked among the top five vendors for the highest bailment and other warehouse charges incurred.

SLC personnel explained that the Commission continued to purchase the local manufacturer's product for its own warehouse inventory after the conversion to the bailment warehouse beginning in December 1990. In March 1992, the SLC ceased purchasing the product for its own warehouse inventory but allowed the manufacturer to store product in the Concord warehouse without bailment or other fees for up to ten days. Since the bailment warehouse has been operating, all other manufacturers are required by the SLC to maintain a two-month supply of product in the warehouse and pay bailment, shipping, and handling charges.

From March 1992, warehouse charges were generated but accounts payable staff were instructed by SLC management not to mail invoices to the local manufacturer. According to SLC management personnel, the 10-day limit has been exceeded as many as 20 times in a year with no financial repercussions. Further, no controls exist to determine if the manufacturer's products are kept to a 10-day inventory level; the MIS division is not providing this service. SLC warehouse personnel have explained that no other vendors are treated in this manner.

OBSERVATION NO 29: PREFERENTIAL TREATMENT OF LOCAL LIQUOR MANUFACTURER (Continued)

SLC commissioners and the financial management director, citing RSA 176:12 and administrative rule Liq 309.02, indicated preferential treatment of the local manufacturer was allowed by State law and liquor rules. Our interpretation of RSA 176:12 and Liq 309.02 is that preferential treatment for New Hampshire products is allowed only in listing and delisting and is not extended to the bailment warehouse.

The United States Constitution Article I, § 8, authorizes the Congress to regulate commerce among the States. In 1983 the United States Supreme Court ruled, in Bacchus Imports, Ltd., v. Dias, Director of Taxation of Hawaii, that states may not discriminate in purpose or effect against out-of-state products or in favor of local products. Further, the Justices interpreted the central purpose of the twenty-first amendment as, "not to empower States to favor local liquor industry by erecting barriers to competition."

The SLC has not treated all manufacturers of alcoholic beverages uniformly regarding the bailment warehouse operation. The State of New Hampshire could become subject to liability based on the U.S. Supreme Court decision in Bacchus Imports, Ltd., v. Dias. Further, the State has lost $345,780.98 in bailment income.

RECOMMENDATION:

We recommend the attorney general investigate whether the SLC violated any State or federal laws pertaining to treatment of manufacturers of alcoholic beverages. We further recommend the SLC immediately require the local manufacturer to pay bailment and other warehouse charges incurred from this point forward and seek reimbursement for bailment and other warehouse charges incurred from March 1992 to the present.

AUDITEE RESPONSE:

The SLC concurs in part. For the complete text of the SLC's response, see Appendix D, page D-71.

For attorney general response, see Appendix E.

4.2 MARKETING AND SALES

Within the marketing and sales divisions we identified two control weaknesses in store operations and two others in the warehouse. First, the store operations policies and procedures manual is outdated and does not reflect procedures followed by store personnel. Further, store personnel were not complying with all security procedures. We also identified building security and inventory controls as problem areas in the warehouse. The Concord warehouse operates under an "honor system," meaning security measures, such as monitoring of employees leaving the warehouse and visitor access are minimal. Also, supervisory review of warehouse employees and inventory controls need improvement.

OBSERVATION NO. 30: INSUFFICIENT COMPLIANCE WITH STORE OPERATIONS MANUAL

We found State liquor store personnel did not have a comprehensive and up-to-date manual to provide guidance on SLC policies and procedures. The current SLC store operations manual, which details procedures to be followed by State liquor store employees, was written in 1987. The store operations manual needed revision to reflect current store practices. The SLC chairman stated in February 1994 the store operations manual needed to be updated and anticipated manual revisions to be complete before summer. As of May 1994 the manual had not been updated. We identified several sections of the 1987 store operations manual that needed revision:

- Cash control and security - the manual does not reflect current bank deposit procedures and does not detail procedures for redeeming merchandise certificates.

- Inventory control - manual procedures are not current with inventory taking procedures which use Telxon scanners and in-store processors, nor with the new shelf management program.

- Buildings and equipment - the manual does not include procedures for requesting repairs or servicing of store equipment by the maintenance supervisor and remodeling crew.

- Building security - the manual does not detail entry and exit protocol for stores with burglar alarms including repercussions for employee-caused false alarms resulting in fees charged by local police departments.

Bank deposit procedures in particular needed to be clarified. The procedure in the manual requires informing local police of night deposits and asking for an escort when available. One supervisor/manager stated there no longer was a need for police escorts at night because credit card sales have reduced the amount of cash in deposits. Another supervisor/manager reported police in his city charge for escorts. Store operations and financial management personnel reported that night deposits require two people going to the bank. The store operations manual makes no mention of this

4. MANAGEMENT CONTROLS (Continued)

4.2 MARKETING AND SALES (Continued)

OBSERVATION NO. 30: INSUFFICIENT COMPLIANCE WITH STORE OPERATIONS MANUAL (Continued)

requirement, yet most supervisor/managers we interviewed indicated awareness of the two-person requirement. However, six of the eight managers and one of the four supervisor/managers we interviewed reported making one-person night deposits despite this requirement.

Store managers also were not following important security procedures in the store operations manual. For example, on separate occasions LBA auditors observed a former liquor commissioner and liquor salespersons in the back rooms of State liquor stores. Also, during visits to State liquor and wine outlet stores, LBA auditors observed large case displays that blocked the view of customer areas by store employees.

The commissioners reported that only SLC employees are allowed in the back rooms of State liquor stores. The store operations manual states that customers, liquor salespeople, friends, or former employees are not allowed in the back rooms of stores. The manual also states that case displays and point of sale materials should not block an employee's view of customer areas.

Allowing unauthorized personnel into the back rooms of State stores exposes the State to unnecessary risk by allowing unauthorized access to product inventory. Unauthorized personnel may also distract store employees from observing customers. While large displays further product sales, the size of the displays should not interfere with a store employee's view of customer areas. Both situations create opportunities for losses to occur.

Policies and procedures in the store operations manual are not being enforced by SLC management. Since 1992 one commissioner has placed added emphasis on store employees building more and bigger displays in State stores to increase product sales.

RECOMMENDATION:

The SLC should reevaluate policies and procedures in store operations to determine continued applicability and necessity. Where necessary store operations should revise the manual to reflect current practices and procedures in the State stores. Upon completion, the updated store operations manual should be distributed to all 68 State liquor and wine outlet stores and all store employees should receive in-service training regarding the manual. Store operations should ensure compliance with policies and procedures in the store operations manual. Displays should be designed so as not to block employee views of customer areas. Store supervisors should assess compliance with policies and procedures while on supervisory visits.

4. MANAGEMENT CONTROLS (Continued)

4.2 MARKETING AND SALES (Continued)

OBSERVATION NO. 30: INSUFFICIENT COMPLIANCE WITH STORE OPERATIONS MANUAL (Continued)

AUDITEE RESPONSE:

The SLC concurs in part. For the complete text of the SLC's response, see Appendix D, page D-72.

OBSERVATION NO. 31: POLICIES AND PROCEDURES NEEDED FOR DEPOSIT WITHHOLDINGS

Managers of State liquor and wine outlet stores are withholding money from Friday bank deposits to ensure sufficient funds are available to make change on weekends and holidays. According to financial management personnel, an average of 14 of the 68 store managers report to financial management on Friday as to what amounts are going to be withheld from bank deposits. Store managers make deposits on the following Sunday evening for that day's sales plus the withheld amounts to compensate for the Friday deposit. Financial management personnel keep track of this practice to ensure the Sunday deposit reconciles with the shorted Friday deposit.

According to the SLC's chief accountant, the change fund amounts authorized by Governor and Council are insufficient. Governor and Council has authorized $68,000 to be used by the SLC for a petty cash and change fund. Of this total $62,050 is used by State liquor and wine outlet stores to make change. The last time Governor and Council authorized an increase in the SLC petty cash and change fund was on June 24, 1992.

The ability of State liquor and wine outlet stores to operate effectively and efficiently is impeded when sufficient money is not available to make change on weekends and holidays. By withholding money from bank deposits, store managers are in effect temporarily increasing the change fund without approval from Governor and Council.

The SLC chief accountant reported that Governor and Council has declined to increase the SLC petty cash and change fund in recent years because it is viewed as unnecessary. Managers of State liquor and wine outlet stores are withholding money from Friday evening bank deposits because they want to ensure enough cash is available over the weekend to make change for customers. Store employees cannot go to banks on Sundays and holidays for change since the banks are not open for business.

4. MANAGEMENT CONTROLS (Continued)

4.2 MARKETING AND SALES (Continued)

OBSERVATION NO. 31: POLICIES AND PROCEDURES NEEDED FOR DEPOSIT WITHHOLDINGS (Continued)

RECOMMENDATION:

The SLC should request an increase in the petty cash and change fund from Governor and Council. In addition, the SLC should develop written policies and procedures regarding deposits withheld to accompany the Governor and Council request. The policies and procedures should include necessary management controls.

AUDITEE RESPONSE:

The SLC concurs. For the complete text of the SLC's response, see Appendix D, page D-74.

OBSERVATION NO. 32: SECURITY OF STATE LIQUOR AND WINE OUTLET STORES MAY BE INSUFFICIENT

We interviewed management personnel at 12 State stores. All eight managers and four supervisor/managers interviewed voiced security concerns and identified areas where physical security needed improvements. Store personnel pointed out weak doors, and the absence of alarms for front and back doors, as well as for display windows. Management personnel spoke of recent night time break-ins in which store safes containing change funds were stolen. In addition, one store manager cited a break-in in December 1993 that left the back door damaged. As of March 21, 1994 the door had not been repaired. Two managers and two supervisor/managers identified a need for holdup alarms at registers. Two supervisor/managers and one manager reported problems with alarm systems at their stores, especially with false alarms.

RECOMMENDATION:

The SLC should conduct a thorough security audit of its 68 stores and implement additional security measures specific to each store location where warranted.

AUDITEE RESPONSE:

The SLC concurs. For the complete text of the SLC's response, see Appendix D, page D-75.

4.2 MARKETING AND SALES (Continued)

OBSERVATION NO. 33: INSUFFICIENT SECURITY FOR CONCORD WAREHOUSE

We found the Concord warehouse to be operating without sufficient security. Warehouse entry and exit by employees and outside parties were not being adequately controlled and all warehouse doors were not being monitored by the security contractor.

Contracted security services for the Concord warehouse consisted of maintenance and monitoring of burglar alarms. The enforcement and regulation chief, while acknowledging theft in the warehouse is a concern, also indicated that warehouse security improvements would not be addressed in the SLC's short term security plans.

Warehouse management reported that the Concord warehouse operated under an "honor system" and all employees exit through one door. Other SLC personnel expressed concern over warehouse security. A store manager cited a situation where boxes of product were missing promotional items such as t-shirts when received from the Concord warehouse. One commissioner observed warehouse employees leaving the Concord warehouse at closing time with coats over their arms; warehouse management were not present at the door. In another case, a warehouse employee fell asleep in the warehouse and was locked in. SLC employees observed a tool handle holding ajar the door that adjoins the main SLC offices to the warehouse. According to one SLC manager, this door has a security access panel intended to control who is allowed into the warehouse but warehouse employees have not been reprimanded for leaving the door unsecured. Because there is a glass door that leads outdoors, near the adjoining door, SLC personnel are concerned with the security of warehouse product.

Finally, the SLC had an exterior warehouse door installed to provide entry to a woodshop. SLC personnel reported this door was not linked to the security system and was installed because maintenance employees work later hours than warehouse employees. An interior sliding door from the woodshop to the inside of the warehouse also exists. This interior door allows access to the rest of the warehouse and had no security control devices.

The SLC is vulnerable to higher amounts of theft and greater security risks in the Concord warehouse than is necessary. The SLC may also be subject to potential legal liabilities if it does not take reasonable precautions to ensure the safety of State employees and property.

The SLC has not made warehouse security a priority. The warehouse and transportation superintendent has not sufficiently monitored employee entry and exit points.

OBSERVATION NO. 33: INSUFFICIENT SECURITY FOR CONCORD WAREHOUSE (Continued)

RECOMMENDATION:

Security improvements in the Concord warehouse should be addressed immediately. Warehouse management should know who is in the warehouse at all times. Outside parties with business at the Concord warehouse should enter and exit through the door near the warehouse administrative offices. Warehouse management should also use sign-in forms for outside parties. Time of entry and exit to the Concord warehouse should be noted. The exterior glass door near the door adjoining the main office and Concord warehouse, as well as the adjoining door, should be equipped with security card access panels from both sides. If the adjoining door also serves as an emergency exit for warehouse personnel a crash bar should be installed on the warehouse side of this door. The exterior woodshop door should also be equipped with security card access panels from both sides. All other warehouse doors should be modified (or replaced if necessary) to become 24 hour emergency doors, including the interior sliding woodshop door.

AUDITEE RESPONSE:

The SLC concurs in part. For the complete text of the SLC's response, see Appendix D, page D-77.

OBSERVATION NO. 34: INSUFFICIENT SUPERVISORY REVIEW IN CONCORD WAREHOUSE

Lack of adequate supervisory review in the warehouse is costing the SLC time and money. From FY 1988 to FY 1994, the Concord warehouse experienced $527,104 in losses and breakage. Of that amount $334,459 was assumed to be due to theft from the warehouse, while $192,645 was due to breakage. Insufficient supervisory review of receiving, data entry, inventory management, storage, and shipping procedures in the warehouse may be responsible for losses carried on the automated warehouse inventory management system. As the following illustrate there are several points at which warehouse employees are in a position to commit or conceal errors:

- No supervisory review occurs when product is received by the warehouse unless there is a discrepancy involving 100 cases or more. Supervisory personnel were not reconciling receiver reports to trucking company manifests.

- Data entry controls on the computer system only check that the quantity entered is no greater than four digits, and that the brand name and receiver report identification number correspond

4. MANAGEMENT CONTROLS (Continued)

4.2 MARKETING AND SALES (Continued)

OBSERVATION NO. 34: INSUFFICIENT SUPERVISORY REVIEW IN CONCORD WAREHOUSE (Continued)

correctly when entered into the system. Product code and quantity may be entered into the computer system incorrectly and go undetected. The inventory tracking system may not be accurate because warehouse management and senior personnel do not conduct supervisory review of data input.

- After store orders have been picked for shipping, additional data adjustments must be made when too many labels have been printed for product not in inventory. However, there was no supervisory review of these adjustments. Nor were orders picked by warehouse personnel inspected by a supervisor prior to shipment.

- Procedures for locating product reported missing by stores when they receive shipments are not always timely. SLC personnel indicated that because orders are picked on an on-going basis, searches for missing product have been delayed for six months. Warehouse management stated that 85 to 90 percent of missing cases are later found in the Concord warehouse. These cases could have been shipped to another store and returned to the warehouse or never shipped at all.

- Perpetual warehouse inventory is only compared to physical warehouse inventory once a year. Interim inventories, such as cycle counts, would aid management in identifying and rectifying inventory discrepancies throughout the year, strengthening overall inventory tracking and management procedures.

- Store and warehouse personnel reported product breakage was higher than it should be because warehouse management does not supervise how pallets are stacked for warehouse storage or shipment to stores. Store and warehouse personnel reported that pallets tip over because cases with glass bottles are stacked on top of cases with plastic bottles. In addition, cases are not interlocked or secured with shrink wrap; instead electrical tape is often used ineffectively.

Sound business practices require conducting and documenting multiple levels of supervisory review in a timely manner. Supervisory review minimizes the possibilities for human error, inefficient practices, possible fraud, and possible abuse. Written guidance helps to ensure mutual understanding of operations and responsibilities between staff and management, assigns accountability, and assists with the continuity of operations over time.

4.2 MARKETING AND SALES (Continued)

OBSERVATION NO. 34: INSUFFICIENT SUPERVISORY REVIEW IN CONCORD WAREHOUSE (Continued)

RECOMMENDATION:

Supervisory review of receiving, data entry, inventory management, storage, and shipping activities should be strengthened by warehouse management. Policies and procedures should be developed and implemented regarding warehouse supervisory reviews. Interim comparisons of perpetual to physical warehouse inventory levels should be conducted.

AUDITEE RESPONSE:

The SLC concurs in part. For the complete text of the SLC's response, see Appendix D, page D-79.

4.3 ADMINISTRATIVE SUPPORT

As described earlier, SLC administrative support functions are the responsibility of financial management, MIS, and human resources administration. We observed control weaknesses in both financial management and MIS. For financial management these weaknesses include insufficient policies and procedures, insufficient management oversight, and questionable practices. We also found insufficient policies and procedures in MIS, insufficient supervisory review, and lack of formal planning and top management oversight for the division. In section 3 we detailed a number of management weaknesses in the human resources function. While we do not present in this section any control weaknesses, a possibly fraudulent action involving human resource administration was discussed in Observations No. 27 and No. 28 of the current section.

OBSERVATION NO. 35: FINANCIAL MANAGEMENT POLICIES AND PROCEDURES INSUFFICIENTLY DOCUMENTED

Financial management is responsible for all financial transactions of the SLC including all accounting functions, documenting and tracking revenue transferred to the State Treasury Department, paying the SLC's bills, and employee payroll. The division is comprised of four sub-units: (1) general ledger, (2) accounts receivable, (3) accounts payable, and (4) payroll.

We observed that controls were not adequately documented or communicated to financial management personnel. Written policies and procedures did not exist during our audit fieldwork. Two employees reported being unaware of

OBSERVATION NO. 35: FINANCIAL MANAGEMENT POLICIES AND PROCEDURES INSUFFICIENTLY DOCUMENTED (Continued)

the reasons why they perform specific daily tasks. We also found cases where employees were not following division procedures, such as sending out and documenting overdue notices to licensees with SLC credit accounts. We also observed that file management procedures were insufficient.

Government Auditing Standards issued by the Comptroller General of the United States identify policies and procedures as essential to the control structure of an agency. Policies and procedures provide reasonable assurance of an agency's ability to record, process, summarize, and report financial data, as well as comply with laws and regulations. In addition, written policies and procedures are basic management requirements. Written guidance ensures mutual understanding of operations and responsibilities between staff and management, minimizes training time for management when hiring new staff, assigns accountability, and assists with the continuity of operations over time.

We found that financial management was without written operating policies and procedures to govern its daily activities. The financial management director had not made the development and implementation of policies and procedures a priority. The director reported the SLC follows the State personnel rules and there was no need for policies in many areas since some personnel had been employed by the SLC a long time and knew the procedures. However, the director later delegated policies and procedures development to the supervisor of the general ledger unit in December 1993.

As of April 1994, only the accounts receivable policies and procedures were near completion, while the general ledger, accounts payable, and payroll policies and procedures had not been developed. The financial management director indicated the supervisor of the general ledger unit had detected several unforeseen problems in each unit where specific policies had to be created before the policies could be written down.

Some financial management personnel reported concerns regarding the lack of written policies and procedures in specific areas such as payroll, accounts receivable, credit cards, and accounts payable. One manager reported supervisory review and checks used to minimize human error, inefficient practices, possible fraud, and possible abuse were inadequate. Several personnel indicated policies and procedures were wanted and needed.

OBSERVATION NO. 35: FINANCIAL MANAGEMENT POLICIES AND PROCEDURES INSUFFICIENTLY DOCUMENTED (Continued)

In addition, SLC personnel were not adequately documenting certain financial transactions. The petty cash and change fund was not reconciled by financial management personnel prior to January 1994. No documentation of overdue notices and credit approvals for licensees was completed prior to February 1994. The financial management director stated he would have difficulty proving the basis for granting credit approval to licensees if ever asked.

File management procedures in particular did not allow for easy review of petty cash and change fund reimbursement requests, receipts, or backup documentation to ensure the petty cash and change fund was properly reimbursed. For example, financial management personnel were not maintaining a separate file which documents all monthly petty cash expenditures. Instead, once monthly reimbursement requests were calculated, all backup documents were being separated and placed alphabetically in general files. As a result, SLC personnel could not easily locate backup information for petty cash and change fund transactions.

Financial management personnel were unable to provide all documentation requested for travel vouchers submitted by commissioners from FY 1990-1993 and training records or logs for FY 1988-1993. Maintaining training records and logs can help managers determine training already participated in by employees and identify other employees who may need to attend training courses offered in the future.

Without written operating policies and procedures, staff may be unclear about management expectations. Job awareness helps employees visualize final results and identify ways to improve their job. Further, lack of policies and procedures makes it difficult to document substandard employee performance.

RECOMMENDATION:

The financial management director should develop and implement written, comprehensive operating policies and procedures. This process should include reviewing the informal practices currently in existence and defining goals and standards for more effective management. The policies and procedures that are developed should reflect levels of supervisory review, management controls, and documentation requirements. All financial management staff should receive in-service training on the policies and procedures. A separate file should be kept with supporting documentation of monthly petty cash disbursements and reconciliation statements.

OBSERVATION NO. 35: FINANCIAL MANAGEMENT POLICIES AND PROCEDURES INSUFFICIENTLY DOCUMENTED (Continued)

RECOMMENDATION: (Continued)

Training records for division personnel should be accurately maintained. The financial management director should communicate documentation procedures to personnel and ensure procedures are implemented by financial management supervisors.

AUDITEE RESPONSE:

The SLC concurs in part. For the complete text of the SLC's response, see Appendix D, page D-83.

OBSERVATION NO. 36: INSUFFICIENT SUPERVISORY REVIEW

We found insufficient management oversight by the financial management director, chief accountant, and three of four unit supervisors. We also found untimely reconciliations and reviews of general ledger transactions. As of January 1994 reconciliations were six months behind.

Sound business practices require conducting and documenting multiple levels of supervisory review in a timely manner. Supervisory review minimizes the possibilities for human error, inefficient practices, possible fraud, and possible abuse. This measure also provides a level of accountability for actions taken by employees and direction given by supervisors. Sound business practices also require timely reconciliation of financial transactions.

Three of the four unit supervisors were not conducting adequate review and documentation of work completed by employees under their supervision (the fourth supervisor had been conducting reviews of all units since February 1994). Financial management employees, particularly those in receipt of cash and checks, as well as those completing licensee credit approvals and credit card functions, were in a position to conceal errors or irregularities. The SLC was not taking all reasonable precautions available to minimize the potential for human error, inefficient practices, possible fraud, and possible abuse.

Financial managers attempted to compare internally generated general ledger transaction reports to transaction reports generated by the Bureau of Accounts within the Department of Administrative Services. By completing such comparisons errors could be detected and reconciliations made. However, management controls must be timely to be effective. At June 28,

OBSERVATION NO. 36: INSUFFICIENT SUPERVISORY REVIEW (Continued)

1994, bank statement reconciliations for credit card transactions had not been completed for the previous ten months. At January 29, 1994 reconciliations for SLC general ledger financial transactions were behind by six months. Because reconciliations were so far behind, errors or irregularities could remain undetected by SLC management for several months.

Insufficient supervisory review in financial management was occurring because the financial management director had not been actively ensuring that the chief accountant and unit supervisors conduct and document appropriate reviews. According to SLC management, lack of written procedures regarding reconciliation of financial information prevented division personnel from understanding and completing reconciliations in a timely manner. Financial management personnel reported that the director was not keeping division employees apprised of their responsibilities. The director was not ensuring that assigned employees get caught up on reconciliations or assigning additional personnel to assist. The financial management director reported that he did not view daily financial operations as part of his job responsibilities and that he viewed himself as more valuable to the SLC regarding policy decisions.

RECOMMENDATION:

The financial management director should ensure that all unit supervisors conduct adequate review and documentation of the work of all accounting employees within their units and that the chief accountant adequately supervises the work of the unit supervisors. The financial management director should also ensure timely reconciliation of credit card and general ledger transactions.

AUDITEE RESPONSE:

The SLC concurs in part. For the complete text of the SLC's response, see Appendix D, page D-84.

OBSERVATION NO. 37: INAPPROPRIATE USE OF PETTY CASH AND CHANGE FUND

The SLC used its petty cash and change fund to inappropriately pay for many expenses instead of following normal procedures established for State agencies. Also, the SLC in effect transferred funds among program appropriation units (PAUs) to reimburse some of those expenses without first obtaining necessary approvals by the Fiscal Committee and Governor and Council.

OBSERVATION NO. 37: INAPPROPRIATE USE OF PETTY CASH AND CHANGE FUND (Continued)

Procedures are set up in State government to pay for expenses incurred by State agencies so that petty cash funds do not have to be used as the SLC has used its petty cash and change fund. Such procedures include the completion and submission of State travel vouchers to the Department of Administrative Services (DAS) and use of requisitions and purchase orders with the assistance of the Division of Purchase and Property.

We reviewed numerous SLC petty cash expenditures for the period March 23, 1987 to February 28, 1994. We questioned 46 disbursements totaling $13,827.17 from the SLC petty cash and change fund. These include the following: (1) 13 payments totaling $5,295.57 for travel and mileage, (2) six payments totaling $4,195 for training, (3) five payments totaling $2,217.10 for conference costs, and (4) 22 payments totaling $2,119.50 for miscellaneous items including automotive parts and repairs, business lunches, and a special tax registration fee to the federal Bureau of Alcohol, Tobacco, and Firearms. Almost half of the questioned disbursements involved commissioners or SLC division directors.

After disbursements were made from the petty cash and change fund, the SLC completed internal accounting transactions to reimburse the fund from the PAU that originally incurred the expenses. However, in some cases expenses were reimbursed from PAUs that did not incur them. For example, a reimbursement for a plane ticket in the amount of $251.00 was initially paid to a liquor commissioner from petty cash. SLC financial management personnel attempted to reimburse $251.00 from funds appropriated for out-of-state travel for the office of the commissioners (PAU code 1010, class code 80) but there were insufficient funds available. The balance was reimbursed from funds appropriated for in-state travel for financial management (PAU code 1023, class code 70).

Although the SLC does not have written policies and procedures to govern the use of the petty cash and change fund, common sense and DAS procedures should be used in deciding what expenses should be paid out of this fund.

According to administrative rule Adm 304.04 (expired), State agency employees must fill out a travel payment voucher (form A-4) to be reimbursed for private vehicle travel, common carrier travel, meals, hotel, and other miscellaneous expenses. One commissioner repeatedly submitted mileage and other travel expense information on note pad paper, not travel voucher forms. Financial management personnel would tabulate total mileage amounts and reimburse the commissioner with a check from the petty cash and change fund.

OBSERVATION NO. 37: INAPPROPRIATE USE OF PETTY CASH AND CHANGE FUND (Continued)

Administrative rule Adm 308.03 (d)(1)(a)(b) (expired) states an overnight stay is necessary to be reimbursed for meals. There were at least two petty cash disbursements for business lunches where an overnight stay was not involved.

Administrative rule Adm 311.06 (expired) requires agencies to submit written estimates to the Bureau of Purchase and Property along with a requisition for work to be done to repair motor vehicles. This procedure is followed when it is not possible to procure firm competitive bids for repairs to motor vehicles. The SLC made at least four petty cash disbursements to a liquor investigator for automotive parts, repairs, or both.

The petty cash and change fund is being used inappropriately. The SLC has overridden State management controls to pay travel, training, conference, and other expenses from the petty cash and change fund. Program appropriation units that have not incurred expenses are paying expenses incurred by other PAUs.

SLC commissioners and division directors circumvented normal State authorization and reimbursement procedures for convenience. According to SLC management, one commissioner wanted immediate reimbursement for travel expenses incurred and did not want to wait for travel voucher forms to be processed. An SLC manager reported being unaware that the SLC could request approval from DAS to transfer appropriated funds among PAUs.

RECOMMENDATION:

The SLC should develop written policies and procedures on the purpose and use of the petty cash and change fund. The policies and procedures should be distributed to all SLC personnel. Management controls over the petty cash and change fund should be enforced by the financial management director. The financial management director should consult with the SLC business supervisor at the Department of Administrative Services regarding the transfer of appropriated funds so that the budgetary needs of the SLC may be more effectively managed.

AUDITEE RESPONSE:

The SLC concurs. For the complete text of the SLC's response, see Appendix D, page D-88.

4. MANAGEMENT CONTROLS (Continued)

4.3 ADMINISTRATIVE SUPPORT (Continued)

OBSERVATION NO. 38: INSUFFICIENT SECURITY FOR CASH AND CHECKS

In a 1989 LBA financial audit of the SLC, it was recommended that a restrictive endorsement be placed on all checks when they are received. The LBA recommended that the restrictive endorsement be stamped by the person who receives the payment, either in hand or through the mail. This recommendation was not fully implemented as evidenced by interviews with SLC personnel and a memorandum issued from the SLC general ledger unit supervisor on April 4, 1994. In this memorandum, the supervisor directed all SLC employees who receive any checks to stamp the checks with a restrictive endorsement immediately upon receipt.

In addition, we found general ledger personnel were not consistently or adequately securing cash and checks received from other SLC divisions or licensees. Cash and checks were not always secured in a locking bank bag or the SLC safe located near the payroll unit. One clerk reported leaving cash and checks on her desk during the day, even when on breaks and out to lunch. The clerk stated that she occasionally will ask another employee in the area to watch her desk. The same clerk also reported that checks she received from other SLC divisions were not consistently stamped with a restrictive endorsement. This was verified by other SLC personnel. In addition, an administrative supervisor stated receipts were not issued by financial management personnel for cash and checks placed in the safe near the payroll unit. Finally, we observed that the safe located near the payroll unit was routinely left unlocked throughout the day and no permission was required to get into the safe. According to SLC personnel, no one at the SLC checks to see what goes into or comes out of the safe throughout the day.

By not securing cash and checks in employee work areas, as well as the safe near the payroll unit, the SLC has allowed a security risk to be created and jeopardized property of the State and its employees. For example, one SLC employee reported seeing another employee's paycheck in the safe near the payroll unit and remarked how easy it would be to walk away with other employees' paychecks.

Financial management has insufficient management controls over cash and checks received by employees in the general ledger unit. Government Auditing Standards issued by the United States Comptroller General identify policies and procedures as essential to the control structure of an agency. Specific standards regarding internal controls of an organization stipulate that access to resources and records be limited to authorized individuals, and accountability for the custody and use of resources be assigned and maintained.

4. MANAGEMENT CONTROLS (Continued)

4.3 ADMINISTRATIVE SUPPORT (Continued)

OBSERVATION NO. 38: INSUFFICIENT SECURITY FOR CASH AND CHECKS (Continued)

RECOMMENDATION:

The financial management director should develop, implement, and enforce policies and procedures regarding cash and checks received by the general ledger unit and any other applicable units. These policies and procedures should include management controls requiring employees to maintain security over cash and checks at all times.

AUDITEE RESPONSE:

The SLC concurs in part. For the complete text of the SLC's response, see Appendix D, page D-89.

OBSERVATION NO. 39: DISPOSITION OF PRINTER PURCHASED THROUGH SHELF MANAGEMENT CONTRACT IS QUESTIONABLE

The MIS director spent $3,094 to purchase a specialized printer, an X-Y plotter, as part of the shelf management development contract he received from the SLC. The printer was placed in the MIS director's office at the SLC. The MIS director provided documents demonstrating that he billed the SLC separately for the plotter. Financial management personnel reported the plotter was not on the fixed asset inventory because they believed it did not belong to the SLC. The MIS director reported the printer was SLC property but acknowledged that since it was not purchased in the normal fashion, it would not show up on normal printouts of equipment. We agree with the MIS director that the SLC owns the plotter since it was paid and accounted for separately under the shelf management development contract.

RECOMMENDATION:

Financial management should ensure the X-Y plotter is placed on the SLC's fixed asset inventory.

AUDITEE RESPONSE:

The SLC concurs. For the complete text of the SLC's response, see Appendix D, page D-93.

4. MANAGEMENT CONTROLS (Continued)

4.3 ADMINISTRATIVE SUPPORT (Continued)

OBSERVATION NO. 40: INSUFFICIENT MANAGEMENT INFORMATION SYSTEMS POLICIES AND OVERSIGHT

The data processing function at the SLC incorporates a very large and complex system, with hardware units located in each of the State liquor and wine outlet stores, the warehouses in Concord and Nashua, and the SLC offices in Concord. All store locations and the warehouses are on-line with the SLC offices, and in the case of the stores can provide real time sales data. These data are used to determine when store inventories should be replenished, tracking sales information from prior years, as well as reconciling daily sales information.

MIS supports other SLC functions by maintaining computer systems, developing programs, providing in-house software training, and generating informational reports. During the course of our audit MIS personnel were involved in multiple projects such as testing computerized store cash registers to accept new sales promotion information, creating an enforcement violations database, developing a store-wide shelf management program to optimize sales, as well as coordinating inventory taking and control efforts for the SLC.

We observed that MIS had been operating without sufficient guidance or oversight by the commissioners. This was evidenced by insufficient internal planning documents and the lack of an information technology plan as required by State law. MIS did not have comprehensive written operating policies and procedures to govern operations and activities such as program development and testing. Due to the extensiveness and diversity of MIS involvement in overall operations it is essential for top management in the SLC to be setting and prioritizing objectives for this support function.

Policies and procedures are basic management requirements. Written guidance ensures mutual understanding of operations and responsibilities between staff and management, minimizes training time when hiring new staff, assigns accountability, and assists with the continuity of operations over time.

MIS did not have comprehensive written operating policies and procedures to govern operations and activities such as program development and testing. MIS-related policies and guidelines that we reviewed pertained to acquisition, security, and maintenance of computer equipment and software, as well as user requests for assistance and specialized computer training. MIS personnel reported that store-based computer systems were minimally tested and that there were no standard testing criteria for programs and systems developed in-house. Personnel also reported that consistent standards on user and system documentation were needed.

OBSERVATION NO. 40: INSUFFICIENT MANAGEMENT INFORMATION SYSTEMS POLICIES AND OVERSIGHT (Continued)

Without written policies and procedures, MIS staff may be unclear about management expectations, store-based computer systems may not be sufficiently tested, and inventory controls may not be consistently used. Further, the lack of written policies and procedures makes it difficult to document substandard employee performance and to take disciplinary actions where warranted.

In addition, MIS had not developed an information technology plan in accordance with RSA 9:4-b. The development plan provided to LBA auditors by the MIS director consisted of a one-page list of projects and calendar dates. Missing from the plan was any descriptive information about the projects or details regarding staffing assignments, contingencies, funding requirements, or priority assignments.

According to RSA 9:4-b, each executive department must prepare an information technology plan which includes budget data for both new information technology initiatives and existing operations. Further, the agency must follow the process developed by the director of the Office of Information Technology Management (OITM).

One commissioner reported no formal planning session with MIS had ever occurred and that direction for MIS was not supplied by the commissioners, but rather by what computer users wanted or needed. The MIS director and other personnel indicated commissioners provided little or no oversight of the MIS Division. Some MIS personnel indicated more direction by the commissioners was needed. One MIS manager noted commissioners have not indicated where MIS should be in the next five years.

MIS has been operating without sufficient guidance or oversight by the commission. Furthermore, the lack of internal formal and directed planning, as well as failure to develop an information technology plan, may result in the insufficient identification of SLC technology needs, inefficient use of agency resources, lack of direction, and insufficient support by the MIS. The SLC developed its management information system independent of other State agencies and as a result has not benefitted from other agency experiences with and expertise on computer software and hardware.

OBSERVATION NO. 40: INSUFFICIENT MANAGEMENT INFORMATION SYSTEMS POLICIES AND OVERSIGHT (Continued)

RECOMMENDATION:

The commission should take an active role overseeing MIS activities. MIS should work with OITM to develop an information technology plan in accordance with RSA 9:4-b. The commissioners, with the active participation of the division directors, should identify the direction, purpose, and goals of MIS for the SLC. The information technology plan should discuss the development and acquisition, enhancement, and maintenance of software supporting sales, administrative, and enforcement purposes, as well as hardware in the stores, warehouse, and central offices of the commission.

The MIS director should develop and implement comprehensive written operating policies and procedures. Upon completion, all MIS personnel should receive in-service training on written policies and procedures.

AUDITEE RESPONSE:

The SLC concurs. For the complete text of the SLC's response, see Appendix D, page D-94.

OBSERVATION NO. 41: INSUFFICIENT SUPERVISION OF INVENTORY TRACKING PROCEDURES

We found the SLC was not adequately tracking product inventory or adequately reconciling inventory discrepancies. Product shortages reported by stores, if never found, are assumed to be due to theft. From FY 1988 to FY 1994 the SLC identified and attempted to track potential losses of approximately $3.4 million and potential overages of $2.1 million. In actuality it was unknown how much may be due to data entry mistakes by store operations or MIS personnel. Furthermore, store operations and MIS personnel were in a position to commit and conceal errors when entering and correcting information in SLC computers.

We also determined that while it was reasonable for MIS to provide the central tracking support for all SLC product, it was not reasonable that corrections made by MIS personnel to inventory databases were not subject to supervisory review. We concluded that data entry mistakes made by store and MIS personnel were translated to product shortages and incorrectly assumed to be due to theft.

4. MANAGEMENT CONTROLS (Continued)

4.3 ADMINISTRATIVE SUPPORT (Continued)

OBSERVATION NO. 41: INSUFFICIENT SUPERVISION OF INVENTORY TRACKING PROCEDURES (Continued)

Store managers adjust inventory levels on in-store processors when they receive more or less product than listed on packing slips. Store personnel may also be directed by the MIS Division to input information into their computers when discrepancy amounts entered previously are subsequently found to be incorrect. However, supervisor/managers were not reviewing load receiving summaries and packing slips to ensure correct data entry by store personnel.

MIS also maintains databases to track store discrepancies and perpetual inventories. However, computerized inventory levels may not accurately reflect actual store inventory levels because corrections made by MIS personnel are also not subject to supervisory review. Further, MIS personnel were not comparing load receiving summaries to store packing slips upon receipt from stores. Rather, division personnel rely on weekly cycle inventories to pick up errors made by store employees, increasing the total number of codes store personnel must count. As a result, the amount of time used by store personnel to conduct cycle counts is higher than necessary.

Sound business practice requires accurate inventory levels in order to effectively sell product. Supervisory reviews completed in a timely manner minimize possibilities for human error, inefficient practices, possible fraud, and possible abuse.

RECOMMENDATION:

Supervisor/managers should reconcile printed discrepancies reflected in load receiving summaries to packing slips when visiting stores every two weeks. Doing so would provide a higher level of accountability for store personnel and better ensure the accuracy of discrepancies inputted into in-store processors. Copies of load receiving summaries and packing slips should still be sent to MIS because it serves as a central tracking point for all SLC product. MIS corrections to discrepancies reported by stores should be reviewed for accuracy by the MIS director or another MIS supervisor who did not complete the correction.

AUDITEE RESPONSE:

The SLC concurs in part. For the complete text of the SLC's response, see Appendix D, page D-96.

4. MANAGEMENT CONTROLS (Continued)

4.4 ENFORCEMENT AND REGULATION

As part of its responsibilities related to issuing licenses and enforcing State liquor laws, the Enforcement and Regulation Division serves as the primary collection point for license fees and administrative fines issued by the SLC. Division investigators do not accept payments from licensees when in the field, rather fees and fines are delivered to the SLC office in Concord by mail or personally by the licensee. We determined that procedures for processing fines and fees received by enforcement and regulation were not sufficient and should be improved. In particular, restrictive endorsements were not immediately placed on checks, receipts for cash placed in the financial management safe were not always obtained, data entry of fine payments received, as well as bank deposits of fine payments, were not verified. Further, records for 3,486 licensees including background and violation information, were not secured during or after business hours in a locking filing cabinet.

<u>OBSERVATION NO. 42: INADEQUATE PROCEDURES FOR PROCESSING LICENSE FEES AND FINES</u>

The Enforcement and Regulation Division does not have adequate policies and procedures relative to receiving, recording, and processing licensee fees and fines.

A financial management general ledger account clerk is responsible for processing fine payments through the SLC accounting system. However, no one in financial management or enforcement verifies that the account clerk entered the information into the computer or that the checks and cash were deposited into an SLC bank account.

According to the account clerk, when she receives a check for a fine through the mail she does not inform anyone in enforcement that a licensee has paid an outstanding fine.

According to enforcement management the receptionist at the front desk was not stamping a restrictive endorsement on checks she received from walk-in customers (this issue was also discussed in Observation No. 38). The administrative supervisor responsible for processing license fees also does not stamp checks she receives until she is ready to input new applications and renewals into the computer. If the administrative supervisor enters the wrong license fee amount, the computer will not process the transaction until the correct amount is entered.

OBSERVATION NO. 42: INADEQUATE PROCEDURES FOR PROCESSING LICENSE FEES AND FINES (Continued)

The computer used in the Enforcement and Regulation Division is incapable of accepting information on fines. According to the administrative supervisor there are no data entry controls for entering fine amounts by the general ledger account clerk. The account clerk in the general ledger unit does not know why she is responsible for reviewing data entry done by the administrative supervisor or why she must enter information pertaining to fines paid.

In addition, the administrative supervisor in enforcement places large amounts of cash upon receipt in the safe located in financial management. The administrative supervisor stated the safe was not always locked and she did not get a receipt for cash put in the safe at these times. (However, when the administrative supervisor brings all cash and checks received from payees to the general ledger unit at 2:30 p.m. daily, a receipt is issued by an account clerk in that unit.)

Written policies and procedures are basic management requirements. Written guidance helps to ensure mutual understanding of operations and responsibilities between staff and management, minimizes training time for management when hiring new staff, assigns accountability, and assists with the continuity of operations over time. Policies and procedures provide reasonable assurance of an agency's ability to record, process, summarize, and report financial data, as well as comply with laws and regulations.

Without written policies and procedures, as well as other management controls, enforcement and regulation cannot ensure the proper receipt and recording of license fees or fines. Levels of supervisory review and types of checks used by the SLC to process license fees and fines are not sufficient to minimize the potential for human error, inefficient practices, possible fraud, and possible abuse. Further, if the general ledger account clerk does not notify enforcement personnel that outstanding fines were paid by licensees, vendor licenses may be wrongfully suspended.

The enforcement chief has not made the development and implementation of written policies and procedures pertaining to processing fees and fines a priority.

4. MANAGEMENT CONTROLS (Continued)

4.4 ENFORCEMENT AND REGULATION (Continued)

OBSERVATION NO. 42: INADEQUATE PROCEDURES FOR PROCESSING LICENSE FEES AND FINES (Continued)

RECOMMENDATION:

Personnel in the Enforcement and Regulation Division should complete the data entry requirements necessary to clear paid fines. The division chief should consult with MIS to complete software modifications necessary for payment information on fines to be entered into the accounting system using computers in the Enforcement and Regulation Division. The chief should also develop and implement written policies and procedures to ensure the proper receipt and recording of license fees and fines. Enforcement personnel should obtain receipts anytime cash is put in the safe located in financial management.

AUDITEE RESPONSE:

The SLC concurs. For the complete text of the SLC's response, see Appendix D, page D-98.

OBSERVATION NO. 43: ENFORCEMENT AND REGULATION DIVISION LICENSEE RECORDS ARE NEITHER SECURE NOR COMPLETE

RSA 178:2 requires the SLC to "keep a full record of all applications for licenses, of all recommendations for and remonstrances against the granting of licenses, and of the action taken on such applications." In addition, RSA 5:33 (I) requires agency heads to be responsible for establishing and maintaining economical and efficient management of agency records. Records should contain proper, adequate documentation of the organization's procedures, transactions and functions necessary to protect the legal and financial rights of the state and of persons affected by the agency.

As of March 28, 1994, the Enforcement and Regulation Division reported 3,486 active licenses, including vendors, distributors and clubs. The Enforcement and Regulation Division maintains licensee records, including license applications and renewals, supporting documentation, violations of liquor laws, fines issued, and other information. Licensee records are not secure. The division's main filing cabinet containing them is not locked; division personnel do not have keys for the cabinet, nor do they know if the lock works. The cabinet was given to the SLC by another agency. File security is complicated by the location of the office of the human resources administrator (HRA). The HRA is adjacent to enforcement. Visitors to the HRA must walk directly past unsecured licensee files. The potential exists for licensee file information tampering or theft. Lost or incomplete

OBSERVATION NO. 43: ENFORCEMENT AND REGULATION DIVISION LICENSEE RECORDS ARE NEITHER SECURE NOR COMPLETE (Continued)

documentation, or tampered files may impede ongoing or future investigations, interfere with hearings, or complicate licensee renewals. Legal rights of the State as well as persons affected by the commission may be jeopardized.

The enforcement chief expressed general concern regarding office security. However, neither he nor the administrative assistant chief perceived a file security problem until some files we requested could not be located. Furthermore, the chief and administrative assistant chief stated that some licensee files are incomplete. The division is attempting to obtain missing file documentation such as corporate minutes documenting corporate office personnel changes, corporate by-laws, affidavits on corporate officials regarding felony convictions, licensee proof of control over licensee premises, and registration names for non-corporate licensees.

The enforcement chief reported wanting to maintain more file information on failed businesses to protect the State's legal rights. In the past only the application was kept. However, the chief has not recommended changes in the division's record-keeping requirements to the SLC commissioners.

RECOMMENDATION:

The SLC should repair or replace the current Enforcement and Regulation Division licensee records file cabinet with a locking cabinet.

Procedures regarding file security and access should be developed. At a minimum, these procedures should include the following: (1) key access determined by the enforcement chief; (2) files secured and file cabinet locked at the close of each business day; (3) enforcement personnel strictly control file access by outside parties, ensuring that all files are returned intact; (4) files signed out and signed back into the Enforcement and Regulation Division; (5) the chief and the administrative secretary supervisor responsible for maintaining strict file control access; and (6) visitors to the HRA escorted at all times while in the enforcement work areas, unescorted visitors should be directed to wait at the SLC visitor sign-in counter.

Additionally, the Enforcement and Regulation Division should take steps to ensure that its files are accurate and complete. The division should develop and implement a formal, structured file system, that will enable users of the files to more efficiently locate needed information. The file system should include a table of contents sheet, as well as directions for making file adjustments or corrections.

OBSERVATION NO. 43: ENFORCEMENT AND REGULATION DIVISION LICENSEE RECORDS ARE NEITHER SECURE NOR COMPLETE (Continued)

AUDITEE RESPONSE:

The SLC concurs in part. For the complete text of the SLC's response, see Appendix D, page D-99.

4.5 COMPLIANCE

We identified three areas where the SLC has not adopted administrative rules: (1) the operation of the Concord bailment warehouse, (2) the assessment of administrative fines and licensee suspensions, and (3) specifying when exceptions to rules may be granted. In all three areas the SLC interacts with third parties outside State government, such as a licensee or vendor representative, and as a result is required by RSA 541-A:1(XV)(b) to implement administrative rules.

As part of our compliance review of applicable State and Federal statutes we determined that the SLC will be violating federal cooperative advertising regulations if proposed rule modifications are implemented by the federal Bureau of Alcohol, Tobacco, and Firearms. Further, more is being spent on SLC in-state media advertising than allowed by RSA 175:4(III)(b). We determined this is inconsistent with the law's intent and clarification of this State statute should be pursued by the SLC to adjust its advertising campaigns accordingly.

OBSERVATION NO. 44: ADDITIONAL ADMINISTRATIVE RULES SHOULD BE PROMULGATED

According to RSA 541-A:1(XV)(b) an administrative rule prescribes or interprets "an agency policy, procedure or practice requirement binding on persons outside the agency..." including the general public. In addition, RSA 541-A:16(I,b) requires each agency adopt rules of practice, in addition to other statutory rulemaking requirements, that set forth the "nature and requirement of all formal and informal procedures available...." We found the SLC has failed to promulgate administrative rules in three areas.

First, the SLC has not adopted administrative rules for the Concord bailment warehouse since it went into operation in December 1990. By not promulgating administrative rules the SLC has failed to formally identify and notify how it will interact with the liquor and wine manufacturers and vendors with which it does business.

OBSERVATION NO. 44: ADDITIONAL ADMINISTRATIVE RULES SHOULD BE PROMULGATED (Continued)

Second, the SLC has not adopted administrative rules regarding the assessment of fines and the suspension of licenses. The Enforcement and Regulation Division uses a schedule for assessing administrative fines which is based on a schedule used by the courts. Additionally, the division has adopted a general policy of suspending a license, when the licensee fails to pay fines incurred within ten days of receipt of the division's penalty letter. As a result, the commission has imposed a schedule of administrative fines and a 10-day payment rule without due notification as required by RSA 541-A.

RSA 179:57 (I) grants the SLC authority to fine or suspend licensees but the 10-day limit prior to suspension is not specified. The law also allows the SLC to levy fines no less than $100 nor more than $5,000 for any one offense. However, criteria to determine which offenses should incur higher penalties, are not specified in the statute or administrative rules.

Third, on different occasions the SLC has allowed special exceptions to administrative rules regarding wine tastings. In these circumstances vendors and their representatives were allowed to offer at wine-tastings wines not sold by the SLC. In one situation the SLC allowed the vendor representative to specify to the SLC what the SLC's mark-up would be. The vendor representative then submitted payment in the amount of the mark-ups that he calculated.

On previous occasions this vendor had violated SLC statutes regarding wines. On June 2, 1992, the vendor conducted wine tastings with uncoded brands and solicited orders. Although conducting a wine tasting without purchasing the wines through the SLC was a violation of RSA 179:32, the vendor representative was not sanctioned for the offense. Almost one year later, on April 19, 1993 the SLC fined the vendor's representative $250.00 for selling wine directly to a licensee without going through the SLC. We are concerned that commissioners are suspending or making special exceptions to SLC rules without sufficient authority to do so.

RECOMMENDATION:

The SLC should develop administrative rules pertaining to the bailment warehouse system and adopt them according to RSA 541-A. At a minimum these rules should explain the types of charges levied for storing product in bailment, how the charges are calculated, case storage limits, as well as other restrictions that may apply.

4. MANAGEMENT CONTROLS (Continued)

4.5 COMPLIANCE (Continued)

OBSERVATION NO. 44: ADDITIONAL ADMINISTRATIVE RULES SHOULD BE PROMULGATED (Continued)

RECOMMENDATION (Continued):

The SLC should adopt administrative rules pertaining to administrative fines and suspensions for failure to pay fines in a timely manner.

The SLC should adopt and follow administrative rules specifying when and under what conditions exceptions to rules will be made in order to better ensure all licensees are treated the same.

AUDITEE RESPONSE:

The SLC concurs in part. For the complete text of the SLC's response, see Appendix D, page D-102.

OBSERVATION NO. 45: COOPERATIVE ADVERTISING

Approximately 14 times each year liquor industry members purchase advertisements in the Manchester Union Leader. The advertisements often appear in full-page size with as many as five full pages in a single advertisement and with each full page containing 15-20 "spots" (each spot costing an average of $181.66). The advertisements state that they were "... [P]laced and paid for by the individual liquor distillers, not the State Liquor Commission." Directly below the disclaimer in large type appear the words "State Liquor & Wine Outlet Stores" and "NH Liquor Commission." This part of the advertisement is paid for by the commission. Similar advertisements are placed in the Boston Globe less frequently.

At other times smaller advertisements from individual industry members appear on different pages throughout the newspaper simply listing SLC product codes and the sale price without any mention of where the product may be purchased. Interspersed with these smaller advertisements is at least one similar in all respects but with the addition of an SLC tagline.

Employees for the Union Leader and the Globe explained that they sell these advertisements directly to the industry members. An SLC employee and a newspaper employee reported that the SLC supplies the newspapers with information concerning SLC sale of the month price lists and approves the advertisements before they appear.

OBSERVATION NO. 45: COOPERATIVE ADVERTISING (Continued)

The Federal Alcohol Administration Act (the "FAA") states that it is unlawful for any distiller, directly or indirectly, to induce any retailer to purchase products by paying or crediting the retailer for any advertising (27 USC § 205 (b)(4)). Administrative rules issued by the federal Bureau of Alcohol, Tobacco, and Firearms (the "BATF") prohibit cooperative advertising defined as "An arrangement in which an industry member participates with a retailer in paying for an advertisement placed by the retailer ... ." (27 CFR § 6.52). The commission is considered a retailer under the FAA and BATF rules.

In a notice of proposed rulemaking, BATF has proposed that the phrase "placed by the retailer" be deleted from § 6.52 in order to emphasize that it does not matter whether the retailer or industry member places the advertisement (59 Fed. Reg. 80, 21702, April 26, 1994). If this change is approved, the commission will be engaging in and benefitting from cooperative advertising with liquor industry members in violation of the FAA.

RECOMMENDATION:

The commission should either seek a waiver from BATF to allow it to participate openly and directly in cooperative advertising or withdraw its permission for such advertising.

AUDITEE RESPONSE:

The SLC does not concur. For the complete text of the SLC's response, see Appendix D, page D-106.

OBSERVATION NO. 46: CLARIFICATION OF RSA 175:4, ADVERTISING

In FY 1993 SLC in-state media advertising expenditures from funds appropriated by the legislature amounted to approximately $65,852. We estimated the amount spent directly by industry members for liquor advertisements in the Manchester Union Leader was between $38,149 and $108,088. These latter dollars by-pass the normal appropriations process and increase in-state advertising expenditures by anywhere from 58 to 164 percent. When added to the liquor commission's in-state media expenditures, the in-state advertising expenditures of industry members boosted total in-state media spending from 20.4 percent of appropriated dollars to between 28.8 and 40.3 percent.

OBSERVATION NO. 46: CLARIFICATION OF RSA 175:4, ADVERTISING (Continued)

As amended in 1990 and 1991, RSA 175:4 (I) states that "[a]ll advertising of liquor and beverages is prohibited unless specifically authorized by the commission." RSA 175:4 (II) authorizes the commission to advertise and regulate advertisement of liquor and beverages through "newspapers, magazines, periodicals, television and radio broadcasting, sports films and travelogs." RSA 175:4 (III) requires funds appropriated to the commission for the purposes of paragraph I be expended 80 percent for liquor advertising with out-of-state media; and 20 percent for liquor advertising with media in the State.

The law was also amended in 1976. That amendment (SB 9) increased the annual appropriation from $10,000 to $50,000 and revised the split between out-of-state and in-state advertising from 50-50 to 80-20. A review of discussions by legislators in both houses shows that opponents of the measure were concerned with issues of control and in-state advertising. Proponents of the bill successfully argued that increased advertising was being sought primarily to combat a growing threat of competition from Massachusetts.

The 1976 statute had the first and second paragraphs in the current statute reversed. As a result, paragraph III referred to the commission's authority to advertise, as well as to regulate advertising. The current statute appears to limit the commission's authorized expenditure to activities relative to authorizing all advertising.

The commission may be violating the intent of the State law requiring an 80-20 split between out-of-state and in-state advertising. By cooperating with industry members in their placing significant amounts of advertising in in-state newspapers, the commission is exceeding statutory intent to limit in-state advertising expenditures.

RECOMMENDATION:

The SLC should request clarification of statutory intent regarding RSA 175:4.

AUDITEE RESPONSE:

The SLC does not concur. For the complete text of the SLC's response, see Appendix D, page D-108.

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STATE OF NEW HAMPSHIRE
STATE LIQUOR COMMISSION

CONCLUSION

5. CONCLUSION

The State Liquor Commission has always been a dependable source of revenue for State government. Over the six year period of our audit, FY 1988 to FY 1993, the SLC transferred over $308 million to the State's general fund. But the liquor monopoly's proportional contribution has been on the wane reflecting a national trend. Americans have become more health and safety conscious and as a consequence are consuming less alcohol. That behavior has translated into purchases of more wine and less liquor. The results have been felt at SLC cash registers and ultimately in the State's general fund.

In FY 1988 the SLC transferred over $45.1 million to a general fund that had revenues of $641.4 million. The SLC contribution amounted to 7.0 percent of general fund revenue. By FY 1994 general fund revenue from all sources had increased 96.5 percent to $1.26 billion while the SLC transfer had increased only 26.1 percent to $56.9 million. This amounted to a smaller 4.5 percent share of general fund revenue.

The SLC has attempted to respond to its diminishing role in State government and the changing behavior of its customers by refurbishing many of its stores and putting forth a greater effort in marketing wine, it shows signs of being either unable or unwilling to adequately cope with its status as a State agency. This inability or unwillingness is manifested in findings documenting potential fraud and abuse as well as a cumbersome and inefficient organization without clear policies and procedures and without adequate planning and leadership.

The SLC allowed administrative units responsible for financial management, personnel administration, and computerized management information systems to rely on antiquated accounting software to manage a business with $208 million a year in sales; allowed a no-bid contract to be awarded to an SLC manager; allowed a part-time employee with political connections to be given health and medical benefits contrary to State policy; and allowed thousands of dollars of purchases to escape normal State oversight by willfully circumventing established, written procurement policies.

Units responsible for marketing, merchandising, and store operations have not kept pace with personnel and customer needs regarding supervision, staffing, training, and safety. Market planning, analysis, and advertising efforts need to be reviewed and, where necessary, improved. Enforcement and regulation responsibilities are not as effective as they could be because of inefficient deployment of supervision, training, and staff.

5. CONCLUSION (Continued)

Therefore, we have two conclusions. First, several SLC practices we observed (Observation Nos. 21-29) should be reviewed by the attorney general. Second, if the SLC is to increase its efficiency and improve services to its customers, thereby increasing sales and revenue to the State, it needs management changes the Legislature has determined are appropriate for other State agencies: a single commissioner, stronger administrative support, and a streamlined marketing and sales operation.

STATE OF NEW HAMPSHIRE
STATE LIQUOR COMMISSION

OTHER ISSUES AND CONCERNS

In this section we present two minor observations, as well as another issue reviewed during our audit which were not developed into formal observations. While these issues are subordinate to concerns expressed in prior sections of this report, we do consider these issues noteworthy. The SLC, the Legislature, and the Executive Branch may consider these issues and concerns deserving of action or further study; therefore we have included suggestions where appropriate.

REPEAL OF RSA 176:5, BOND REQUIREMENT

RSA 176:5 requires liquor commissioners to be bonded in the amount of $10,000 each. However, this statutory requirement is unnecessary since the liquor commissioners are covered by the State's Faithful Performance Blanket Position Bond.

The Faithful Performance Blanket Position Bond covers all State employees for losses due to the failure of its employees to faithfully execute their duties, or to properly account for money and property received in the course of their employment. The limit for each unscheduled employee is $100,000 with a deductible of $1,000 per employee. The administrator of the State's Risk Management Program confirmed that the State's Faithful Performance Blanket Bond provides coverage for liquor commissioners.

We recommend the repeal of RSA 176:5 since the commissioners are covered under the State's Faithful Performance Blanket Position Bond. The Commission concurs with our recommendation and will submit a request to the Legislature to repeal RSA 176:5 in the upcoming session.

NONCOMPLIANCE WITH ANNUAL REPORT REQUIREMENT

RSA 20:7 requires the SLC to submit an annual report to Governor and Council. The SLC develops annual financial statements. However, we observed the SLC does not provide narrative discussions and analyses of its performance from year to year in terms specified by Department of Administrative Services' rules. According to administrative rules 317.01 and 317.02 (expired), agencies must submit annual reports or biennial reports in a standard format. Administrative rule 317.01 states that agencies should place "an emphasis on functional results and accomplishments rather than fiscal facts since the commissioner's, treasurer's, and budgetary reports fully reflect fiscal matters." Agency reports should explicitly state the statutory requirements of the agency, as identified in RSA 176:3, and how these statutory requirements are being accomplished. Because the SLC does not standardize its annual report both the executive and legislative branches of government, as well as the public cannot easily discern the SLC's performance from year to year.

NONCOMPLIANCE WITH ANNUAL REPORT REQUIREMENT (Continued)

We recommend the SLC work with the Department of Administrative Services to develop an annual report in accordance with administrative rules 317.01 and 317.02. We also recommend the SLC set internal performance goals and objectives by division and annually evaluate whether these benchmarks have been achieved. The results of these evaluations should be included in annual reports.

The Commission has indicated the FY 1994 Annual Report will be in full compliance with Adm 317.

PAST TRANSFERS OF STORE EMPLOYEES FROM ONE STORE TO ANOTHER

The Enforcement and Regulation Division developed procedures in December 1993 to address suspected employee theft. Prior to the implementation of these procedures the only mechanism used for dealing with such suspected theft consisted of transferring store employees to other locations. For example, in 1991 approximately $27,000 in product was stolen from the Plaistow store (#49). In 1993 approximately $6,000 in product was stolen from one of the Manchester stores (#31). SLC personnel reported that in both cases the MIS Division detected the losses through inventory controls, the Enforcement and Regulation Division was notified, and all of the store's employees were transferred to other stores.

According to SLC personnel these transfers were used to deter additional theft, as well as to track any subsequent theft that might occur wherever a suspected employee was transferred. However, we have concerns and questions regarding the effectiveness of this policy since its use in the Plaistow and Manchester stores did not result in the apprehension of any SLC employees suspected of theft. The SLC, in effect, punished employees who were not blameworthy while at the same time it provided little incentive for other employees not to engage in theft. Similar concerns were expressed by two SLC commissioners describing this policy as "not appropriate" and as "punishing the innocent." Although these concerns were expressed we were not informed by the Commission this policy would cease in the future.

Finally, the SLC may have violated Division of Personnel administrative rules by using this policy as a disciplinary measure. Permanently transferring employees as a form of punishment conflicts with Per 302.02 (a), (b). According to these rules the SLC needed to obtain permission from the director of the Division of Personnel <u>before</u> permanently transferring employees. Further, reasons for the proposed transfer should have been related to job functions and <u>not</u> as a measure with punitive intent. We suggest the SLC cease using the transfer policy and consult with the Division of Personnel to determine acceptable disciplinary measures. Procedures developed in December 1993 should be expanded to include disciplinary measures and then be communicated to all SLC personnel.

APPENDIX A

CONTROL AND LICENSE STATES IN NEW ENGLAND

CONTROL STATES	LICENSE STATES
Maine	Connecticut
New Hampshire	Massachusetts
Vermont	Rhode Island
Source: Distilled Spirits Council of the United States, Inc.	

Liquor Control Systems

As demonstrated in the above table, there are three control states and three license states in New England. Along with New Hampshire the control states are Maine and Vermont. The similarities and differences in the alcohol regulatory practices of the New England states are detailed below.

<u>Organizational Structures in Control States</u>

The Maine Department of Public Safety has been responsible for liquor law enforcement since July 1993. The liquor licensing division issues licenses (including agency stores), investigates violations of state liquor laws, collects license fees, and holds all hearings except those pertaining to listing and delisting products for sale in the state, which are the responsibility of the liquor commission.

In April 1994 Maine's Liquor Commission merged with the State's Lottery Commission to form the Maine State Liquor and Lottery Commission. The five-member commission's responsibilities include overseeing the controlled distribution and sale of liquor and lottery products, and conducting hearings pertaining to listing and delisting of liquor products. Maine owns and operates 29 liquor stores; 185 state-licensed agency stores are owned and operated privately.

The Vermont Department of Liquor Control is responsible for regulating that state's alcoholic beverage industry. This department consists of a part-time Liquor Control Board with three members appointed to six-year terms. The board appoints the Department Commissioner. The three board members may be removed for cause.

Similar to New Hampshire, Vermont's liquor board issues licenses, investigates licensees, adopts regulations, and hears appeals. Vermont has nine state-owned and operated liquor stores and 60 agency liquor stores. Vermont enters into private contracts with owners of the agency stores whereby the state receives a commission based on gross sales. Vermont reported it is planning to phase out its nine state stores.

Revenue Raising Systems in Control States

New Hampshire has no tax on retail sales of liquor or other alcoholic beverages per se. However, there is an eight percent meals and rooms tax on alcoholic beverages consumed in restaurants and bars. Also there is a 30 cents per gallon fee on wholesale distributors and beverage manufacturers who sell alcoholic beverages for resale by retail licensees. Furthermore, domestic wine manufacturers pay five percent of their gross revenues to the State; domestic liquor manufacturers have no such requirement.

In contrast, Maine state stores collect six percent sales tax on non-licensee alcoholic beverage sales. The Bureau of Taxation, Sales Tax Division, collects this six percent sales tax on alcoholic beverages sold in agency stores and to licensees. Maine also collects the following excise and premium taxes based on a per gallon measure, as summarized below:

PRODUCT	EXCISE TAX	PREMIUM TAX	TOTAL TAX
Malt beverages	$0.25	$0.10	$0.35
Table wines	0.30	0.30	0.60
Sparkling wines	1.00	0.24	1.24
Fortified wines	1.00	0.24	1.24
Low alcohol spirits	1.00	0.24	1.24
Liquor	varies	1.00/proof gallon	varies

In addition, Maine requires manufacturers of low alcohol spirits to pay an additional $0.30 premium per gallon.

Vermont levies and collects a tax on the sale of fortified wines and spirituous liquors equal to 25 percent of gross revenue. The State's four percent sales tax does not apply to these alcoholic beverages. However, Vermont's sales tax is levied on wine with an alcohol content of 16 percent by volume and beer. Vermont also imposes a ten percent meal tax on alcoholic beverages when consumed on the premises of licensees. Additional fees levied on beer and wine, and collected by the Commissioner of Taxes, include: a 26.5 cents per gallon charge on malt beverages and a 55 cents per gallon charge on natural wines.

Organizational Structures and Revenue Systems in License States

Elsewhere in New England, Connecticut, Massachusetts, and Rhode Island are considered license states. The administrative agency in Connecticut is the Department of Liquor Control, which consists of three commissioners appointed by the Governor. The Department issues licenses, investigates licensees, adopts regulations, and holds hearings. Currently, there are approximately 1,286 licensed package stores (privately owned) throughout Connecticut.

Connecticut taxes alcoholic beverages by the gallon as well as through a retail sales tax. On liquor a $4.50 per gallon tax is applied, while a $2.05 per wine gallon tax for a spirits cooler is imposed. For alcoholic beverages greater than 100 proof a $4.50 tax is applied. Wines with 21 percent or less alcohol receive a 60 cents per gallon fee. An additional $1.50 per gallon fee is imposed on alcohol or sparkling wines having an alcohol content greater than 21 percent. Finally, beer is subject to an excise tax of $1.50 per quarter barrel up to $6.00 per barrel. The retail sales tax applied on alcoholic beverages is six percent.

Massachusetts' administrative agency is known as the Alcoholic Beverages Control Commission. This commission is comprised of a chairman, two associates, and 18 other full-time employees. The two associates are employed on a part-time basis whereas the chairman has a full-time position. The chairman and one associate serve co-terminus with the Governor of Massachusetts for four years. The other associate serves until the middle of the four year term of the other two members of the commission. The Massachusetts Alcoholic Beverages Control Commission issues licenses, investigates licensees, adopts regulations, and holds hearings. There are approximately 2,500 package stores throughout Massachusetts.

Massachusetts taxes alcoholic beverages by the gallon and through its retail sales tax. For malt beverages a $3.30 per barrel charge is imposed. A three cents per wine gallon tax is applied to cider if the alcohol content is three to six percent. Wine is taxed at 55 cents per wine gallon, while sparkling wines are taxed at 70 cents per wine gallon. A $1.10 per wine gallon tax is imposed for products with 15 percent of alcohol by volume or less. If greater than 15 percent alcohol by volume but less than 50 percent, a $4.05 per wine gallon tax results. For products which are greater than 50 percent of alcohol by volume a $4.05 tax per proof gallon is imposed. The general five percent retail sales tax is applied on alcoholic beverages sold for consumption on-premise. There is also a tax amounting to one-half of one percent on gross receipts from the sale of alcoholic beverages and a 14 percent surcharge applies to certain corporations and organizations.

The Liquor Control Administration in Rhode Island is a division of the Department of Business Regulation and is headed by the Liquor Control Administrator. This administrator is appointed by the director of the Department of Business Regulation with the approval of the Governor. The Liquor Control Administration, issues wholesale and manufacturing licenses, investigates licensees, and adopts regulations. However, each city in the

State of Rhode Island issues retail licenses. Currently, there are about 2,000 licensees throughout Rhode Island. Rhode Island has separate agencies to deal with alcoholic beverages-related administrative and adjudicatory activities.

Within the Department of Business Regulation is a three-member Liquor Control Hearing Board. Board members are appointed by the Governor for six year terms and may be removed for cause. The Liquor Control Hearing Board considers appeals from orders of the Department of Business Regulation relating to licenses, rules, and regulations. Rhode Island statute provides that the board is independent and not subject to the supervision of the director of business regulation even though it is part of the department.

Rhode Island has a $3.75 per gallon fee on distilled liquor and brandy. Rhode Island also imposes a $7.50 per gallon fee on beverages manufactured in the state for sale and on ethyl alcohol used for beverage purposes. Further, a $3.00 fee per 31 gallon barrel is placed on beer. Still wines are subject to a 60 cents per gallon fee, and sparkling wines a 75 cents per gallon charge. In addition, a seven percent general retail sales tax is imposed on retail sales of alcoholic beverages.

Regulations on Alcohol Imported for Personal Use

Each state has enacted laws which specify the amount of liquor, wine and beer which may be imported by private persons residing in or traveling through the state without tax liability or permit requirements. The table below summarizes these legal requirements.

STATE	**IMPORT RESTRICTIONS**
New Hampshire	3 quarts liquor or wine; no limit on beer
Maine	4 quarts liquor or wine; 3 gallons beer
Vermont	2 gallons liquor, wine or beer
Connecticut	4 gallons liquor, wine or beer
Massachusetts	0 gallons liquor, wine or beer
Rhode Island	3 gallons liquor, wine or beer

APPENDIX B

STATE LIQUOR STORES - LOCATIONS AND FY 1993 SALES

FY 1993 RANK	STORE NO.	TOWN	LOCATION	FY 1993 SALES	SALES PERCENT	CUMULATIVE SALES	CUMULATIVE PERCENT
1	38	Portsmouth	Traffic Circle	$18,244,516	10.38	$18,244,516	10.38
2	73	Hampton	I-95 South	11,205,362	6.38	29,449,878	16.76
3	34	Salem	South Broadway	9,577,057	5.45	39,026,935	22.21
4	66	Hooksett	I-93 North	7,776,820	4.43	46,803,755	26.64
5	69	Nashua	Coliseum Ave.	7,610,318	4.33	54,414,073	30.97
6	67	Hooksett	I-93 South	6,843,357	3.89	61,257,430	34.86
7	50	Nashua	Southgate	6,673,128	3.80	67,930,558	38.66
8	60	W. Lebanon	Powerhouse Plaza	6,391,626	3.64	74,322,184	42.30
9	15	Keene	Fairbanks Plaza	4,311,742	2.45	78,633,926	44.75
10	23	Conway	Route 16	4,082,406	2.32	82,716,332	47.07
11	52	Gorham	Main St.	3,835,949	2.19	86,552,281	49.26
12	41	Seabrook	Lafayette Blvd	3,667,921	2.09	90,220,202	51.35
13	49	Plaistow	Cedar Brk Plaza	3,491,513	1.99	93,711,715	53.34
14	7	Littleton	Lisbon Rd.	3,215,890	1.83	96,927,605	55.15
15	6	Portsmouth	Portsmouth Plaza	2,971,728	1.69	99,899,333	56.86
16	1	Concord	Storrs St.	2,945,181	1.68	102,844,514	58.54
17	68	N. Hampton	Village Center	2,900,289	1.65	105,744,803	60.19
18	74	Londonderry	Market Basket	2,798,251	1.59	108,543,054	61.78
19	48	Hinsdale	Route 119	2,797,674	1.59	111,340,728	63.37
20	33	Manchester	North Side Plaza	2,602,071	1.48	113,942,799	64.85
21	55	Bedford	Bedford Grove	2,492,093	1.42	116,434,892	66.27
22	14	Rochester	Wakefield St.	2,273,488	1.30	118,708,380	67.57
23	54	Glen	Shopade Center	2,271,403	1.29	120,979,783	68.86
24	56	Gilford	Lakes Plaza	2,228,156	1.27	123,207,939	70.13
25	26	Groveton	Route 3	2,076,572	1.18	125,284,511	71.31
26	31	Manchester	East Side Plaza	2,052,881	1.17	127,337,392	72.48
27	9	Dover	Central Ave.	2,052,802	1.17	129,390,194	73.65
28	30	Milford	Granite Town	1,970,527	1.13	131,360,721	74.78
29	64	New London	Shopping Center	1,906,652	1.09	133,267,373	75.87

FY 1993 RANK	STORE NO.	TOWN	LOCATION	FY 1993 SALES	SALES PERCENT	CUMULATIVE SALES	CUMULATIVE PERCENT
30	25	Exeter	Globe Plaza	1,852,910	1.05	135,120,283	76.92
31	42	Meredith	Old Province Cmn	1,656,491	0.94	136,776,774	77.86
32	53	Hudson	Market Basket	1,636,214	0.93	138,412,988	78.79
33	72	Concord	Fort Eddy Rd.	1,630,946	0.93	140,043,934	79.72
34	51	Pelham	Route 38	1,584,290	0.90	141,628,224	80.62
35	39	Wolfeboro	Center St.	1,549,338	0.88	143,177,562	81.50
36	71	Lee	Traffic Circle	1,492,593	0.85	144,670,155	82.35
37	8	Claremont	Claremont Plaza	1,464,960	0.83	146,135,115	83.18
38	47	N. Woodstock	Main St.	1,453,208	0.83	147,588,323	84.01
39	3	Manchester	St. Mary's Plaza	1,434,395	0.82	149,022,718	84.83
40	19	Plymouth	Tenney Mt. Plaza	1,390,137	0.79	150,412,855	85.62
41	21	Peterborough	202 Village	1,358,482	0.77	151,771,337	86.39
42	63	Winchester	Country Mall	1,356,324	0.77	153,127,661	87.16
43	10	Manchester	Maple St. Mall	1,308,896	0.74	154,436,557	87.90
44	40	Walpole	N. Meadow Plaza	1,251,604	0.71	155,688,161	88.61
45	27	Nashua	Simoneau Plaza	1,234,074	0.70	156,922,235	89.31
46	13	Somersworth	300 Main St.	1,161,215	0.66	158,083,450	89.97
47	61	Fitzwilliam	Routes 12 & 119	1,131,554	0.64	159,215,004	90.61
48	57	Ctr. Ossipee	Indian Mound	1,117,103	0.64	160,332,107	91.25
49	59	Merrimack	Shaw's Plaza	1,065,384	0.61	161,397,491	91.86
50	11	Lebanon	Masacoma St.	1,047,588	0.60	162,445,079	92.46
51	62	Raymond	Route 27	1,035,520	0.59	163,480,599	93.05
52	18	Colebrook	Main St.	1,020,025	0.58	164,500,624	93.63
53	24	Newport	Sugar River	996,589	0.57	165,497,213	94.20
54	75	Belmont	Belknap Mall	985,045	0.56	166,482,258	94.76
55	12	Laconia	Court St.	908,732	0.52	167,390,990	95.28
56	58	Goffstown	Shop N Save	903,614	0.51	168,294,604	95.79
57	35	Hillsboro	Shopping Center	898,467	0.51	169,193,071	96.30
58	17	Franklin	800 Central St.	851,471	0.48	170,044,542	96.78
59	16	Woodsville	Central St.	830,167	0.47	170,874,709	97.25
60	43	Farmington	Tappan St.	768,854	0.44	171,643,563	97.69
61	5	Berlin	Exchange St.	718,581	0.41	172,362,144	98.10

FY 1993 RANK	STORE NO.	TOWN	LOCATION	FY 1993 SALES	SALES PERCENT	CUMULATIVE SALES	CUMULATIVE PERCENT
62	36	Jaffrey	Monadnock Plaza	674,927	0.38	173,037,071	98.48
63	37	Lancaster	202 Main St.	652,084	0.37	173,689,155	98.85
64	46	Ashland	North Main St.	632,229	0.36	174,321,384	99.21
65	45	Pittsfield	Water St.	583,123	0.33	174,904,507	99.54
66	44	Bristol	Lake St.	547,145	0.31	175,451,652	99.85
67	29	Whitefield	Route 3	267,162	0.15	$175,718,814	100.00

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APPENDIX C

STATE LIQUOR COMMISSION
FULL-TIME POSITIONS AND SALARY RANGES
(AS OF 9/16/94)

	Salary Range	Number of Personnel
Office of Commissioners		
Chairman	53,375-68,768	1
Commissioners	47,230-60,571	2
Administrative Assistant II	24,648-29,094	1
Executive Secretary	18,603-21,762	1
Marketing and Merchandising Division		
Administrator I (Director)	34,651-41,340	1
Business Administrator III	34,651-41,340	1
Wine Marketing Specialist	33,150-39,546	1
Informational Representative	26,735-31,649	1
Administrative Secretary	20,085-23,556	1
Data Control Clerk III	18,603-21,762	1
Accounting Technician	18,603-21,762	2
Account Clerk III	16,497-19,324	2
Purchasing Division		
Purchasing Agent	30,362-36,231	1
Store Operations Division		
Administrator I (Director)	34,652-41,340	1
Plant Maintenance Engineer III	28,517-33,758	1
Stores Supervisor/Manager	28,517-33,758	11
Retail Store Manager IV	26,291-31,034	5
Retail Store Manager III	24,211-28,517	30
Retail Store Manager II	22,318-26,147	54
Retail Store Manager I	20,612-24,128	32
Retail Store Clerk II	19,073-22,318	74
Maintenance Mechanic II	18,603-21,762	1
Secretary Stenographer II	16,497-19,325	1
Laborer	15,516-17,451	2
Warehouse and Transportation Division		
Warehouse Superintendent	29,094-34,437	1
Assistant Warehouse Superintendent	22,698-26,735	1
Administrative Assistant I	21,762-25,662	1
Accounting Technician	18,603-21,762	1
Chief Liquor Shipper & Receiver	18,603-21,762	3
Warehouseman	17,180-20,086	9
Account Clerk III	16,497-19,324	1

	Salary Range	Number of Personnel
Financial Management Division		
Administrator III (Director)	41,341-49,316	1
Chief Accountant	33,150-39,546	1
Human Resources Administrator	33,150-39,546	1
Accountant IV	29,094-34,437	1
Accountant II	23,653-27,924	2
Payroll Officer II	21,762-25,662	1
Senior Accounting Technician	20,085-23,556	2
Administrative Secretary	20,085-23,556	1
Accounting Technician	18,603-21,762	4
Word Processor Operator II	18,603-21,762	1
Account Clerk III	16,497-19,324	4
Clerk II	14,547-16,361	1
Data Processing Division		
Director of Data Processing	45,260-54,483	1
Data Processing Project Manager	41,340-49,316	1
Management Systems Administrator II	39,546-47,171	1
Technical Support Specialist III	37,850-45,143	1
MIS Application Programmer II	36,231-43,193	1
MIS Application Programmer I	33,150-39,546	2
Computer Application Programmer II	29,094-34,437	1
Computer Operator Supervisor II	26,735-31,649	1
PC Specialist II	26,735-31,649	1
Computer Operator Supervisor I	24,648-29,094	1
Computer Operator III	21,762-25,662	2
Data Librarian II	20,085-23,556	1
Computer Operator I	17,882-20,924	1
Data Control Clerk II	17,180-20,085	1
Enforcement and Regulation Division		
Chief of Licensing and Enforcement	42,430-50,618	1
Ass't Chief, Liquor Law Enforcement	35,741-42,257	3
Senior Liquor Investigator	30,275-35,741	5
Liquor Commission Examiner II	27,924-33,014	1
Liquor Investigator	27,854-32,847	12
Liquor Commission Examiner I	24,648-29,094	1
Administrative Secretary	20,085-23,556	1
Accounting Technician	18,603-21,762	1
License Clerk	17,882-20,924	1
Word Processor Operator I	16,497-19,325	1
Total		**308**

APPENDIX D

AUDITEE RESPONSES

OBSERVATION NO. 1

THE SLC SHOULD BE HEADED BY A SINGLE COMMISSIONER

AUDITEE RESPONSE:

We do not concur both with the observation nor the proposed recommendation. The audit team seems to be attempting to capture, integrate and encapsulate all their observations within this particular observation, in order to justify a seriously questionable, and rather drastic policy change recommendation. This is done in a manner which expresses condemnation by using strong inflammatory language, while ignoring or not accepting any of the explanations and rebuttals offered. The observations generally are not backed up with specific facts and more often then not, appear to have been the result of interviews with unknowledgeable or often times possibly disgruntled ex-employees. Inherent in most all of these observations is the lack of "real world" business experience as well as a reluctance to view the agency as a revenue center rather than just a simple cost center. Doing so fails to recognize this agency's need to continually change and react in response to market and retail trends in order to remain a viable and successful profitable operation.

Cited as an example of inefficient and ineffective management was the payment of approximately $246,000 in salaries and benefits for three full-time Commissioners. The Commission is set up operationally very similar to private industry, who would utilize a CEO, CPO, and several Senior Vice Presidents. Reducing the Commission by 2 Commissioners would necessitate hiring at least 2 high priced executives as replacements and no doubt at considerably more in salary and benefit dollars.

Lost would be the built in check and balances inherent with three Commissioners which now would require a determined collusion for any successful attempt towards illegal actions. In it's place would leave an individual who could virtually be characterized as a liquor czar, very powerful in an industry involving millions of dollars with no real checks and balances.

Many of the audit recommendations envision idealistic ideas generally not cost effective and which the Commission has eliminated or not deemed appropriate due to six years of budget cutting requirements by the Executive and Legislative bodies.

OBSERVATION NO. 1 (Continued)

Policies and procedures that were allegedly insufficient were re-written and put in place where necessary. Any so-called organizational shortcomings, if in fact they did exist, have been addressed by the hiring of well educated and trained experts and the implementation of better organizational communications and procedures gained as a result of their knowledge and expertise.

This is the proper and most beneficial manner in which to deal with any inefficiencies and shortcomings.

It must be reiterated that the reorganization indicated pursuant to 21-6 in 1983 specifically did not apply to the State Liquor Commission. In fact, the previous Chairman indicated that reorganizing the three member Commission to one was attempted three times during his tenure and has also come up twice during this Chairman's tenure and has failed each time. The most recent occurrence was this past June when the recommendation was defeated significantly on the floor of the house.

In addition to the previously mentioned reasoning not to change the Commission structure is the fact that we act in a quasi-judicial manner. The most effective action involved in deterring abuse in the use and sale of alcohol lies in the fact that those who issue this license may invoke appropriate penalties and also revocation when necessary. To replace this very important function with an unknowledgeable part time citizen board would result in ineffectiveness, indecision and introduce political solutions that tend to diminish public policy goals of moderation and revenue enhancement. This same reasoning applies to their hearing appeals on the listing and delisting of products as well, and includes acting as a hearing body in bailment and other State Liquor Commission operational administrative decisions.

Finally, to portray the Commission as ineffective and wrought with shortcomings is certainly inappropriate. As we outlined in other observations, we noted many operating successes, such as reported by Robert Morris and Associates, a nationally recognized leader in providing business indexes. They indicated that the average operating profit as a percent of sales of the retail liquor stores they surveyed nationally was **1.0% in 1993 compared to our 21.86%**. In fact the SLC out performed the national average liquor store in every reported category including the following examples:

	Indust. Avg.	SLC FY'93
Gross Profit as a Percent of Sales	22.70	28.53
Operating Expense as a Percent of Sales	21.70	8.75
Inventory Turnover	7.30	11.45
Sales to Total Assets	3.70	7.92

OBSERVATION NO. 1 (Continued)

We recognize that there is a difference between control and license states so we compared the SLC's revenue per capita to those of other states as reported by DISCUS in their latest annual report. Control states reported average per capita revenues of $37.57 compared to $36.58 for license states. New Hampshire was the number one control state with per capita revenues of $75.08, more than twice the $36.86, national average for both control and license states.

We also recognize that just because we out perform the entire retail liquor inventory, we should compare ourselves to leaders in other retail operations to see how we stack up. The following compares our operation with retailing giant Wal-Mart, known within the industry for it's operating efficiencies and profitability:

	Wal-Mart	SLC FY'93
Gross Profit as a Percent of Sales	**21.50**	**28.53**
Operating Expense as a Percent of Sales	**15.10**	**8.75**
Inventory Turnover	**6.20**	**11.45**
Sales to Total Assets	**2.70**	**7.92**
Sales per Square Foot	**$279.00**	**$534.46**
Return on Assets	**14.1%**	**216.1%**
Return on Equity	**30.0%**	**633.1%**

It should be apparent by now that by any objective financial measure, the SLC is an extremely efficient and profitable operation.

Further, we have continually been recognized nationally by vendors, trade magazines, etc. as being among the most successful, envied and copied Liquor enterprises in this Country.

LBA REBUTTAL:

We do not agree with the agency's assertion that we interviewed unknowledgeable employees. Government auditing standards require that we do not ask interview respondents questions they are not qualified to answer. Likewise, we do not agree with the agency's statement regarding "possibly disgruntled ex-employees." Contrary to the SLC's inference, we found the ex-employees with whom we spoke to be dedicated and serious about the agency and its work.

We disagree with the agency's claim that replacing two commissioners would be more costly. The agency has been able to attract quality personnel to direct its marketing and sales functions under current salary schedules but not retain them. Absent a Division of Personnel review of the proposed directors of Sales and Marketing and Administrative Services positions, neither we nor the agency are able to state the actual fiscal impact of the

OBSERVATION NO. 1 (Continued)

recommendation. While an increase in salary grades might occur, we would be very surprised if those increases exceeded the salary of two commissioners.

We do not agree with the agency's characterization of the proposed appeals board as unknowledgeable, ineffective, indecisive, and political. We offer the State Parole Board, the Workers' Compensation Appeals Board, the Personnel Appeals Board, the Public Employee Labor Relations Board, and the Transportation Appeals Board as examples of part-time citizen boards which are knowledgeable, effective, and decisive. There would be no more danger of partisan political involvement with a liquor appeals board than there exists with the current Liquor Commission.

We do not dispute the agency's claim regarding overall performance in the area of sales and the cost of doing business. We do question the validity of the comparisons made between a private sector business concern such as Wal-Mart, which has numerous product categories and much more competitive pressure, and the inherently protected, State-owned liquor monopoly.

OBSERVATION NO. 2

THE MARKETING AND SALES FUNCTIONS SHOULD BE REORGANIZED

AUDITEE RESPONSE:

The Commission concurs in part with the observations, but does not concur with the recommendation. The observation cites coordinating and operational deficiencies within sales-related divisions. They indicate that management and supervisory employees report to both the Commissioners and the appropriate division director. The observation reaches the assumption that these deficiencies caused product shortages and outages, resulting in the loss of some sales.

This observation as in Observation No. 3 implies that a different organizational structure will result in optimizing profitability. The Commission does not concur. The response presented in Observation No. 3 for the most part also responds to this observation. It is most apparent that the current structure by any objective financial measure is an extremely efficient and profitable operation. Any and all private and/or public operations can uncover deficiencies that need to be improved upon. However, you do not use a scattering shotgun approach to resolve a specific and unique deficiency. You focus directly on the deficiency and take the appropriate action.

The insufficient notification of upcoming sales and certain product outages occurred primarily as a result of lengthy vacancies in the Director of Marketing position and the development of process familiarity by the new directors hired to fill that position.

In order to correct this deficiency, the Commission has developed a promotional calendar which extends one quarter ahead. In addition, the Commission strongly suggests that vendors maintain a 60-day inventory at all times. The problem occurs when, for whatever reason, they do not. Accordingly, the Commission is developing a report giving us a general average of monthly sales. This average times 2 should be on hand as inventory in stock to be considered for a future sales promotion. A lack of this sufficient inventory would preclude that product from promotional consideration until corrected by the vendor. In addition, Marketing, Purchasing and Stores directors meet weekly to discuss the coordination of all their sales-related activities both for general as well as for promotional.

Finally, supervisors and managers must and do report directly to their immediate supervisors and not to Commissioners. They reported directly to Commissioners only when there was a vacancy in the appropriate director's position. The individual Commissioners do continue to interact as a liaison between divisions, as well as between divisions and the full Commission. This is very common in private industry, with the difference being in titles only and where, for example, the office of the Chief Executive will have a

OBSERVATION NO. 2 (Continued)

CEO, a President and a Chief Operating Officer working as a team. The most modern organizational setup is a matrix which, operationally, closely resembles the way the Commissioners interact with the directors and the directors with other directors.

LBA REBUTTAL:

The major deficiency in the marketing and sales function within the SLC is the "scattering shotgun" organizational structure we observed. The sales and marketing function should be directed by one person with oversight by the agency commissioner. This would increase accountability at the appropriate levels, and increase coordination among the functional subunits. The agency acknowledges lengthy vacancies in the merchandising director's position. The commissioners, as well as past and current merchandising directors, identified the compensation level that goes with the merchandising director's labor grade as problematic in retaining quality personnel. Our recommendation would most likely result in a higher labor grade for the director of sales and marketing, yet still below the compensation level for one commissioner, making the position more attractive to quality professionals and more cost effective for the State.

OBSERVATION NO. 3

ADMINISTRATIVE FUNCTIONS SHOULD BE REORGANIZED

AUDITEE RESPONSE:

The Commission concurs in part with the observation but doesn't concur with the recommendation. The observation sights operational deficiencies within the MIS and Financial Management divisions. These deficiencies are not necessarily a result of an inefficient organizational structure. Other operational issues such as staffing reductions, uncompetitive pay and budgetary constraints contribute directly to control deficiencies outlined in other observations.

This observation cites the commissions statutory obligation to optimize profitability and implies that a different organization structure will facilitate that goal. The commission contends that profitability is already being optimized. This observation, as well as others, provides no statistical industry benchmarks by which the SLC can be objectively compared. According to Robert Morris and Associates, a nationally recognized leader in providing business indexes, the average operating profit as a percent of sales of the retail liquor stores they surveyed was 1.0% in 1993, compared to 21.86% for the SLC. In fact, the SLC out performed the national average liquor store in every reported category including the following examples:

	Indust. Avg.	SLC FY'93
Gross Profit as a Percent of Sales	22.70	28.53
Operating Expense as a Percent of Sales	21.70	8.75
Inventory Turnover	7.30	11.45
Sales to Total Assets	3.70	7.92

We recognize that there is a difference between control and license states so we compared the SLC's revenue per capita to those of other states as reported by DISCUS in their latest annual report. Control states reported average per capita revenues of $37.57 compared to $36.58 for license states. New Hampshire was the number one control state with per capita revenues of $75.08, more than twice the $36.86, national average for both control and license states.

We also recognize that just because we out perform the entire retail liquor industry, we should compare ourselves to leaders in other retail operations to see how we stack up. The following compares our operation with retailing giant Wal-Mart, known within the industry for it's operating efficiencies and profitability:

OBSERVATION NO. 3 (Continued)

	Wal-Mart	SLC FY'93
Gross Profit as a Percent of Sales	21.50	28.53
Operating Expense as a Percent of Sales	15.10	8.75
Inventory Turnover	6.20	11.45
Sales to Total Assets	2.70	7.92
Sales per Square Foot	$279.00	$534.46
Return on Assets	14.1%	216.1%
Return on Equity	30.0%	633.1%

It should be apparent by now that by any objective financial measure, the SLC is an extremely efficient and profitable operation. This doesn't mean that we don't have any control deficiencies. The question is if the savings gained will be greater than the cost of the controls. An example of this would be with shrinkage in stores. Nationally, the average retail liquor store spends .3% of gross sales on store security. If the SLC were to spend the industry average on security the annual cost to the general fund would be $630,000. Currently, the SLC spends less than $50,000, annually on security. Over the past seven years, the average annual inventory shrinkage for the entire operation was only $85,620. How much money should the SLC spend to resolve the "control deficiencies" that allow the $85,620 in annual shrinkage? Maybe this explains why our operating expenses as a percent of sales is so far below the industry norm.

We must reiterate that the Liquor Commission was not included for consideration of reorganization under the Executive Reorganization Act of 1983. Further, the section of statute setting up the personnel, procedures and responsibilities of the various divisions and directors was reviewed and amended in 1987 & 1989 by the legislature. More importantly, in 1990, this section along with all the Title XIII liquor laws was reviewed for all corrections and necessary changes by a joint house and senate committee on recodification. As a result many sections were in fact changed, amendments added and some sections eliminated. This review involved several months and many hours of effort. Needless to say the full legislature approved of this review and its incumbent changes including the committee's recommendation to continue this agency structure.

We believe that the teamwork that we now use to accomplish our tasks is more important than <u>any</u> rigid organizational structure. It is the marketplace to which we need to respond and customer needs on which we must be focused. To the extent that everyone in an organization has that outward focus, it will succeed. To the extent that other government agencies force us into being inner-directed, we misallocate our time and attention. The industry benchmarks of financial success in an increasingly competitive marketplace would be sufficient evidence of success to anyone with enough "real world" business experience to recognize it.

OBSERVATION NO. 3 (Continued)

LBA REBUTTAL:

The agency's scattered organizational structure and the management model practiced by the commissioners are chiefly responsible for the operational deficiencies cited. Our recommendation creating an administrative services director position would rationally organize the administrative support functions within the agency, increase formal accountability at the appropriate levels, and provide more efficient administrative support for agency subunits. It would most likely result in a higher labor grade for the administrative services director, yet still be below the compensation level for one commissioner, making the position more attractive to quality professionals and more cost effective for the State.

OBSERVATION NO. 4

THE SUPERVISOR/MANAGER SYSTEM SHOULD BE REPLACED

AUDITEE RESPONSE:

The Commission concurs in part.

The observation contains assumptions and opinions which we feel do not reflect our position on the subject of store supervision and are not substantiated by enough facts.

We would like to address some of the issues contained in this observation to explain our position on this subject.

Of the 11 Supervisor/Manager positions, 9 are currently supervising and managing a base store and a geographic location. The other two positions are addressed in another observation response.

The 1987 Sunset report did not have any comment on our analysis of the Supervisor/Manager concept. In 1989 we established the full 11 Supervisor network system.

The system was set up to provide supervision to a small geographic area. The advantages were to provide timely supervision, cut down on state travel and be able to respond to the needs of each store. It also provided that the Supervisor/Manager would operate a base store, which would keep the Supervisor/Manager abreast of all store procedures and the base store is staffed with permanent employees, qualified to assume the Store Manager duties, and capable staff able to operate the store in the absence of the Supervisor/Manager visiting his or her other stores.

The question to address is what amount of direct supervision we need for our stores. Each store has Managers who are accountable to run a State Liquor Store. The information we provide to each Supervisor/Manager through the central office and our MIS Division provides the information necessary to make intelligent business decisions in the field, it monitors each store's inventory, productivity, etc., so that the operations are monitored on a daily, weekly or monthly basis. The part we want the Supervisor/Manager to accomplish is store visits, to assess the store presentation on cleanliness, merchandising, security and personnel. The financial transactions are monitored by the central office. We provide information to them on any problems encountered with each store. We agree that store audits should be periodically conducted by the Supervisors. Most store problems can be answered by telephone directly through the Supervisor/Manager or an alternate Supervisor/Manager. The network is set up to provide quick response to the stores by the Supervisor/Manager.

OBSERVATION NO. 4 (Continued)

We also agree that during peak periods, such as Christmas, it is difficult for the Supervisor to leave his/her base store, but not impossible since most stores in the area are close by. Since the Supervisor/Manager stores are, in most areas, in close proximity they can be visited early morning or mid afternoon on Tuesday or Wednesday when customers are not active. The Christmas Holiday Season requires weeks of planning; the Store Manager working with the Supervisor/Manager prior to the actual peak business period.

Three former Commissioners commented they were wrong in supporting the Supervisor/Manager System because it did not provide enough supervision for stores responsibilities to manage a liquor store. The Supervisor/Manager System is very dependent on direction and objectives received from the Director of Store Operations which was minimal over the past few years. This would be true under any Supervisory system and with a new Director of Stores that direction is now forthcoming.

There have been significant accomplishments under this present system which is directly attributed to each Supervisor/Manager's accomplishments, just to mention a few: They help train their area stores on the new registers and computer systems, increase store productivity sales/man hours and control store staffing budgets. The elimination of full time positions with more emphasis on part time employees is a cost savings in our operating budget but also creates constant monitoring of staffing needs and expedites decisions at store level. They have done a very credible job under these circumstances. Without an adequate budget for training and development our store operating budgets remaining at level funding for the past few years, one must give much credit to the Managers and Supervisor/Managers.

We are not concerned how other control states run their store operations, we are concerned with how effectively we run ours.

It is also not a fair comparison to judge our Supervisor System against non-liquor private retailers. They do not operate under a State system and have more autonomy on wages and the nature of the business, although its all retail, it is not the same. Our business is much different in that we sell a product that requires special handling at point of sale. Our cashiers and Managers must be thoroughly trained to assure the public's safety and comply with the laws and rules of the State. Unlike most retail operations, the NHSLC has little employee turn-over. The supervision required does not change from store to store.

The Store Operations Division is handicapped because of the budget process. It does not allow us to train and develop our personnel. We need to ensure that Supervisor/Managers can make visits to their stores, we find, in most of the areas, this is not a problem. Store Supervisor/Managers have enough Assistant Managers to delegate responsibilities so they can visit their stores. We do not see this as a major problem.

OBSERVATION NO. 4 (Continued)

To add 6 full supervisors would force us to come up with an additional 5 positions, at the level of Retail Store Manager II, III, or IV which would cost $150,000 without benefits. Some of this would be offset with approximately $15,000 savings in demoting some of the current Supervisory/ Managers. This would also increase in state mileage expenses and, in essence, be too much overhead supervision for what is required, in fact, it may be unproductive use of State funds. This may also create the need for State owned vehicles.

We feel the current system provides adequate supervision for our store operations. It is very cost effective use of man hours and under the direction of the new Director of Stores, we can provide objectives, leadership and direction to meet our overall objections. Whatever problems we have now can be addressed and corrected to provide more effective support to our stores. This current system is adequate for our needs and is cost effective.

We are also implementing a store visit report with check points, and will monitor the results. This will also provide us with data on how effective our Supervisors are and how often they visit stores and what is accomplished during these visits. It will provide accountability for store operations. We can not accept that Supervisor/Managers can not visit stores and oversee the running of the base store. We will provide extra support to the Supervisor/Managers stores if they are not able to visit their stores in a timely basis.

The Supervisor/Manager that is currently acting as the Assistant to the Director of Stores will be submitted to Personnel for reclassification. This position is needed to provide direct support to the Director of Stores.

The Supervisor/Manager working on Shelf Management was working on the Stores program on a temporary basis only and has been re-assigned during this Holiday period to supervising stores.

We fail to see how the establishment of 6 full time Supervisors will be a cost savings that can be measured, nor do we see how this will be more beneficial to our operations over the current system. The Director of Store Operations will continue to monitor the Supervisor/Manager system and recommend improvements or changes when necessary.

LBA REBUTTAL:

Recommendation No. 8 of the 1987 Sunset report states, "Direct the SLC to conduct an evaluation of the 'super manager' system at the end of FY 1987."

Supervisor/managers we interviewed reported that even under normal conditions they are spread too thin, and are unable to do much fine-tuning and merchandising. The stores director reported preferring a district supervisory model consisting of four to five supervisors in the field, with no store management responsibility.

OBSERVATION NO. 4 (Continued)

The agency's rejection of comparisons to other control states and to non-liquor private retail systems is curious in light of several other responses which compare its efficiency with both sectors.

OBSERVATION NO. 5

ENFORCEMENT AND REGULATION DIVISION ASSISTANT CHIEFS SHOULD NOT HAVE CASELOADS

AUDITEE RESPONSE:

We concur in part that in a perfect world with adequate staffing the Assistant Chiefs should not have case loads. The Enforcement Division's high of 24 authorized positions, including the Chief and Assistant Chiefs has been reduced to 21 available positions with many hiring freezes imposed by the executive upon the agency over the past few years. Currently Enforcement is operating with only 19 investigators, including the Chief. During this time it became impractical to have personnel in strictly a supervisory role when Enforcement could not fill vacant positions. At one time there were five actual vacancies which were frozen. To better cope with the work load Assistant Chiefs were assigned territories to augment their greatly reduced supervisory duties (lack of investigators to supervise).

We do not concur in part with the LBA conclusion that there is a breakdown in supervision within the agency which places the state at risk. Investigators are highly trained professional individuals, who have had a minimum 13 week in-house Field Training and Evaluation Program program where new investigators work day to day with a Senior Investigator following a documented training program. The Field Training and Evaluation Program program does not stop at 13 weeks but continues until the recruit successfully completes a 10 week basic police academy program operated by the Police Standards and Training Council. New investigators continue to be closely monitored by their Assistant Chief and are not released from the Field Training and Evaluation Program program until completion of their one year probationary period.

Because of the length and depth of the training programs, investigators, especially those with any appreciable time working for the Commission are highly professional and require <u>very little, if any, day to day supervision</u>. Most problems can be handled by phone. Those situations which require an on site supervisor are easily scheduled by the Assistant Chief as needed.

No one prohibits on-site supervision or aid when needed. Assistant Chiefs can and do schedule meetings or training sessions with investigators when they feel they are needed or when the investigators requests assistance. Newly hired investigators, who have not completed their probationary period receive far more attention than experienced investigators who do not need to have someone ride with them to see how they are working. Sometimes the Education and Training Officer is called upon in unusual cases to perform remedial training in areas where a need has been demonstrated.

OBSERVATION NO. 5 (Continued)

All investigator reports are funnelled through the Assistant Chiefs so they may see both the quantity of activity is produced and the quality of the investigators's work. If problems arise there is adequate flexibility in the current system to meet with investigators and correct problems. Many can be handled telephonically.

Were LBA to recommend that three or more new investigator positions be added to Enforcement to bring our numbers to 24 investigators, it would then make greater sense to have the Assistant Chiefs move into a strictly supervisory role. This would be especially true as the addition of new investigators would result in a more inexperienced work force needing greater direct supervision.

Currently Enforcement conducts East and West or joint investigator meetings where the Assistant Chiefs conduct reviews of new laws and rules as well as setting up procedures to assist subordinates with non-routine or dangerous investigations.

We do not concur that the Education and Training Officer and Administrative Assistant Chief should be reassigned returned to field duty as recommended by LBA. This will be addressed in the response to Observation No. 6.

LBA REBUTTAL:

The Regulation and Enforcement Division chief reported to LBA auditors that he would like the field assistant chiefs to have more supervisory responsibility. He also stated the assistant chiefs' current caseloads are excessive. Also, the assistant chiefs and several investigators reported that the assistant chiefs' caseloads impede sufficient supervision of investigators.

The field assistant chiefs and investigators reported supervision of investigators is inadequate and that meetings are infrequent. No investigator reported regular, frequent nor easily scheduled assistant chief-conducted training.

OBSERVATION NO. 6

THE ADMINISTRATIVE ASSISTANT CHIEF POSITION IS UNNECESSARY

AUDITEE RESPONSE:

We do not concur with your recommendation.

We would like to respond to the observations made in the report.

The Division of Personnel report on the February 1991 establishment of the Administrative Assistant Chief position is incorrectly reported. It was the Liquor Commission's decision, upon recommendation of the Chief of Enforcement, to eliminate the position of Deputy Chief in favor of establishing a third Assistant Chief position at a lower salary grade. The new job description was written to establish this position and approved by the Division of Personnel. The position was posted in house and filled after Personnel's approval and reclassified this position.

The Liquor Commission's reasons for eliminating the Deputy Chief's position was based on several factors one of which was to save money. The other reason was that the Deputy Chief job classification was created many years ago as a back up to the Chief of Enforcement with not enough specific duties, in our opinion, to perform tasks that were necessary to provide direct support in the paramilitary organizational structure of Enforcement or perhaps the wishful thinking of some "heir apparent."

The real need in our organization was to provide help with administrative duties in the central office to assist the Chief of Enforcement in providing coordination of administrative tasks and enforcement tasks to effectively run the Division. When the current Assistant Chief of administration vacancy was posted on May 1, 1991 specifications indicated that it would be responsible for special investigations, internal investigations, monitoring fiscal and budgetary expenditures, administrative rulemaking and covering for the other assistant Chief on leave and other assigned duties.

There was also a need to have some direct control over the auditing section which for years had run somewhat independently of the total Enforcement Division, with only mild overseeing of their duties. This section was drastically reduced in positions and an assessment had to be made in what we were going to accomplish. It became necessary for the Chief and Assistant Chief to evaluate the auditing section and get involved in this area to set goals and parameters on how things would be done vs how things were done. In order to reduce personnel the necessary functions had to be eliminated or be accomplished by cross-training of employees.

Auditing was a typical section set up with rigid parameters in the job specifications with very little cross-training. Each person had specific duties which made them unique, but this built in job knowledge and job security was nontransferable. This concept is fine provided there is no turnover, but in the real world it is not healthy for an organization.

OBSERVATION NO. 6 (Continued)

Having performed their duties well over the years, there was certainly resistance to change or new methods of operation. The Chief of Enforcement wanted to bring this section into the mainstream of the central office. The Administrative Assistant Chief has accomplished this task. Once the Chief of Enforcement determined that cross-training of employees within the enforcement and auditing sections was needed, the division has been able to absorb the reductions without major disruptions. During peak periods the Chief of Enforcement utilized part-time employees, which was unheard of formerly.

The observation allegedly indicated by specialists in the Division of Personnel that it was unnecessary for the administrative Assistant Chief to supervisor office personnel, audit staff, investigators and field assistant chiefs in answering questions.

The Assistant Chief (Administrator) job supplemental was approved by the Division of Personnel to supervise an administrative staff. We do not have this position directly supervise liquor investigators or other field assistant chiefs. In the absence of the Chief of Enforcement these duties are delegated by SOP. The Assistant Chief has direct supervision of training needs with a Senior Investigator, but on the whole the statement made by Personnel is incorrect or the question proposed to them was incorrect.

The observation made by the Division of Personnel that the position of Assistant Chief was unnecessary for a division as small as Licensing and Enforcement is inconsistent with their approval of the supplemental job description and highly inconsistent with classification of job specifications that measure accountability as a criteria not size of an organization.

LBA states that one Assistant Chief does not carry a case load and does not supervise field investigators. The commission, on the contrary, believes that this Assistant Chief does carry a case load, albeit not a traditional one, but in keeping with his supervision of operational functions, out of state licensing, supervision of Commission examiners, the Education and Training Officer and administrative staff.

LBA indicates only a few of the Administrative Assistant Chief's duties, which do not encompass all the duties which are assigned. The position routinely performs licensing investigations and updating of applications for out of state entities, answers correspondence, develops final language for policies and procedures as directed by the Chief and implements those policies and procedures once approved so that the Chief's time may be better utilized for long range planning. The position generally organizes and directs the licensee education and in-house training programs for the store clerks and investigators. The position recommends and determines - in conjunction with the Chief - what training would be appropriate for which investigators at the Police Standards and Training Council.

OBSERVATION NO. 6 (Continued)

The case load involves continuous contacts with prospective licensees from out of state who are seeking licensure in NH, preliminary inquiries for prospective applicants within the state concerning breweries, brew pubs, vendors, liquor and wine representatives and sales persons, wineries, and liquor manufactures or importers.

Supervision is counseling. This Assistant Chief, just as the Chief, counsels investigators on a daily basis on how to handle unusual items and circumstances both in licensing and enforcement. Most of the questions are those of policy, where embarrassment or harm can befall the agency if wrong conclusions are drawn or improper decisions are made. The technical assistance provided to field personnel based on over 20 years of experience with the agency is of the type that even the other Assistant Chiefs call for assistance on technical issues or procedure when in doubt.

In the second paragraph LBA indicates that the Administrative secretary/supervisor conducts performance appraisals on two clerical and the account technician positions. Surely in any corporate structure a vice president does not actively manage the day to day routine affairs nor do individual evaluations of the secretarial pool, even though they may be part of his responsibility. The lower echelon supervisor assigns work, evaluates performance, recommends leave and handles day to day affairs. They do not create policy, change routines, and determine where the company will be in five years, even though good management would consult them on these issues.

LBA seems to imply that there is duplication of the Administrative Secretary Supervisors job description and that of the Administrative Assistant Chief. We believe the wrong inferences have been drawn. The Administrative Secretary Supervisor does provide routine educational enforcement information to licensees and others, the degree of responsibility regarding interpretation of statute or rule is limited and radically different from the accountability and responsibility of the Assistant Chief. She provides answers to the routine, while the Assistant Chief provides or obtains answers to the unusual and unique. We have already addressed various levels of supervision earlier.

The Enforcement Division and the Commission does not concur with the assessment of LBA with regard to the job description of Examiner II. About a year after the selection of the candidate to the position of Examiner III (so called at the time) the title was changed to Examiner II just prior to filling a previously frozen Examiner position.

At the time, the audit section had been decimated by lay offs and elimination of positions. The Word Processor Operator and an Examiner I position had been eliminated. The vacant Examiner II position was frozen and the Account Technician position was not filled (except as part time). When we received the authority to fill the Examiner II (so called at the time) position, it was decided to re-name the Examiners position to I and II respectively as the former Examiner I position has been lost.

OBSERVATION NO. 6 (Continued)

In reviewing the Examiner II functions it was determined that the job description no longer fit the current role. It formerly supervised 5 employees, prior to layoffs and elimination of positions. It was decided to emphasize the training role of the position as it was difficult to justify a supervisory role at labor grade 21 for one position. On March 19, 1992 amended job descriptions were submitted by the Commission to change the responsibilities of Examiner II and Examiner I especially in regard to supervision of non-existent employees to more accurately reflect the responsibilities.

The Division of Personnel observation that the Administrative Assistant Chief and the Examiner II are the same labor grade, would preclude supervision over another employee with the same labor grade is generally an unacceptable practice. We agree in this conceptual interpretation, but there are exceptions to this practice. The position of Administrative Assistant Chief is the same labor grade, but works a 40 hour week with a 171 hour 28 day pay period and makes more money than the normal 37 1/2 hour Examiner II. During the recent request for upgrade, personnel did not believe the labor grade issue was a sufficient reason, when mentioned on appeal, to upgrade the Assistant Chief's labor grade.

On inquiry from the Administrative Assistant Chief, who is currently in the process of an employee evaluation for Examiner II, a copy of the current job specification was requested. It was determined that the changes made by the Commission with regard to the Examiner II position were never processed. (A copy of the request to personnel is included for your edification.)

The Chief of Enforcement and the Commission are prepared to resubmit the changes to the Examiner I and II positions which we thought had occurred.

It can be plainly seen the changes reflect the importance of the training role (both for Examiner I and the Account Technician) and assignment of work by Examiner II with regard to his training responsibilities. In no way does the amended version provide for supervision, evaluation, approval of leave, review of reports/work or discipline except in regard to the trainee.

The observations or comments made by two former commissioners that the position of Administrative Assistant Chief is unnecessary may have been made based on their previous knowledge of the enforcement organization and may be referring to the eliminated Deputy Chief position, which we agree with. We might agree with their assessment of adequate field coverage, which is a primary goal of this agency and we are taking and will take all necessary steps to accomplish this goal. It is difficult for us to assess their comments in light of the changes we have made in our reduction of Administrative staff and reductions in permanent positions. It would be unfair for us to comment on their organizational structure during their tenure.

OBSERVATION NO. 6 (Continued)

LBA states that the Examiners and Administrative Secretary Supervisor should report directly to the Chief. This had been the case until 1983 and it was not working well. Ten years ago it was determined that the work load was impossible to handle by a single person. The legislature sits annually now, the administrative requirements imposed by statute, and the numbers of license application are ever increasing. The only way things have survived and not fallen apart was the more efficient application of the employees to the work needing to be done and greater responsibility for supervision being shifted to the administrative assistant chiefs position.

The current chain of command and supervision in enforcement works better than the system previously tried, which LBA now recommends. Rotating personnel (bringing in assistant chiefs, senior investigators and investigators) does not provide for a continuity of action and requires continuous briefing and debriefing of personnel resulting in lost time and money.

In the final analysis, we do not accept your recommendation to abolish the position of Administrative Assistant Chief based on our assessment of our current needs. We will be flexible enough within the organization to reorganize as the needs of this Division undergo changes and we will not hesitate to address these needs.

LBA REBUTTAL:

The agency's response contains statements that directly contradict those made in responses to Observation Nos. 5 and 7. The administrative assistant chief's position is wasteful and more supervision is needed in the field.

OBSERVATION NO. 7

THE SENIOR LIQUOR INVESTIGATOR LABOR GRADE IS NOT NEEDED

AUDITEE RESPONSE:

We do not concur.

I. LBA indicates that the Senior Investigator Position be abolished and the current positions of Senior Investigator be reclassified to investigator.

We do not concur that the class specification should be abolished. We do not concur with the recommendation that the responsibility for orienting new investigators should be shifted to the Assistant Chiefs. The training and orientation of new liquor investigators must be determined by the Chief of Enforcement, who must consider how many new investigators we have and how most effectively this training should be carried out both in current assignment requirements, work loads and proximity of the investigators area in relation to the trainer required.

We are very cognizant of the Enforcement Division background which is by nature structured by rules and need for structured organization without observation. Some of the observations given to you are reflective of misunderstanding of supervisory delegation with loss of power. Although we can consider these factors we must make our decision to organize and run the Enforcement Division in a manner that can accomplish our organizational goals which is to enforce liquor laws and provide service to our Licenses.

The supplemental job description which was approved by the Division of Personnel lists some supervisory responsibilities for this class specification. The organizational structure for Enforcement has two current assistant chiefs to supervise the entire state, which geographically covers many miles. A lot of this direct supervision for a geographical area is covered through regional meetings and modern day electronic communications networking. The senior investigators in the area are intended to supplement this supervisory chain of command by lending some supervisory support to the investigators in the area as directed by the Assistant Chief. It is almost impossible for the Assistant Chiefs to respond to all direct requests within an area. It is strongly felt that the Senior Investigators fill in the supervisory requirements that are needed in the area. Since the senior investigators are in closer proximity to many of the investigators they can be used for direct access when needed. This allows more supervisory coverage, for the area in enforcement of Title XIII and for our licensed establishments.

Although the Senior Investigator is not continuously supervising subordinates, they are available and are specifically assigned by the Chief in a supervisory role, when the Assistant Chief is on a day off, on vacation, extended sick leave or not available or for special detail such as motorcycle week or when assisting city police departments when they conduct "stings".

OBSERVATION NO. 7 (Continued)

Senior Investigators also provide an informal way for new investigators to acquire job knowledge. Senior Investigators try to foster a mentor relationship with their trainees which last beyond the probationary period, whereby the trainee will feel comfortable to seek counsel or guidance on issues informally, when they might be reluctant to call the office or seek out their Assistant Chief.

In all cases the Senior Investigators have more experience and are utilized to assist Liquor Investigators in their performance of duties and assist the Assistant Chiefs to attain the goals set for the agency. The position fills a very import function to the division. Newly hired investigators cannot be nor are they left to work on their own until they have been certified as police officers by the Police Standards and Training Council and successfully complete phase II of the Field Training and Evaluation Program. Until that time, for liability reasons, no newly hired investigator can work alone because they would not be adequately trained. Assistant Chiefs in their supervisory role cannot very well take a trainee with them when they are going to supervise another investigator or when they are making internal, investigator background or other sensitive investigations.

As recent as October 10, 1990 the Division of Personnel reviewed the position and found it to be viable. There is no doubt in the agency's mind that the position is not only indispensable, but a critical part of the training program of the division.

II. LBA wants responsibility for "orienting" new investigators shifted to the Assistant Chiefs.

On more than one occasion we have hired 3 to 5 new investigators in a short period of time. **There is no way two Assistant Chiefs can handle their supervisory role and at the same time have two or three trainees in tow all at different levels of training**.

By assigning a trainee to a specific Senior Investigator (a Police Standards and Training Council trained Field Training Officer) and by following the progressive stages of the Field Training and Evaluation Program program until completion of Phase II (minimum 13 weeks) the new investigator receives a continuity of training. Once passed into Phase III, the new investigator is released to the supervising Assistant Chief who provides monthly reviews through the duration of the probationary period. This provides the division with a check and balance training program where the Senior Investigator is responsible for the primary in-house training, the Police Standards and Training Council for the recruit's proficiency as a police officer and the Assistant Chief to monitor the results of both programs to ensure that the recruit can do the job prior to being released from their probationary period.

OBSERVATION NO. 7 (Continued)

A single program of training done by the Assistant Chief would have no check and balance, only the Assistant Chief's input as to the level of training and provide a very limited training program if an Assistant Chief had to have 2 to 3 recruits with him at a time and 2 to 3 territories to schedule appointments for and work in at the same time.

A great deal of time and planning went into the Enforcement Division's Field Training and Evaluation Program training program, which is based upon the models presented by Police Standards and Training Council in their Field Training Officer courses. It would be remiss of the Commission to scrap a carefully formulated program and to supplant it with a less comprehensive training program.

III. LBA wants responsibility for coordinating training and education for investigators and other division personnel to repose in a "centralized SLC training officer" (to be detailed later).

This particular aspect is currently being done in the position of the Education and Training Officer, who not only coordinates the day to day Field Training and Evaluation Program program, reviewing the trainers reports and making recommendations for passage to the next phase of training, retraining, remedial training or other appropriate action to insure well trained personnel.

The Division of Personnel established this position at the current Senior Investigator class rather than establish a new classification. While we somewhat agree that responsibility coordinating training and education for investigators and other division personnel should be the responsibility of a centralized SLC training office, the reality of the situation must coincide with the needs for particular training, the time involved, the priority for training and how much training is required. In our assessment much of this is on going and simultaneous. One person could not accomplish all the tasks required.

The Training Officer offers formalized training for on and off-sale licensees in the form of Grocers Education Training Seminar and Total Education in Alcohol Management programs which are conducted in various locations across the state on a continuing basis as well as individual Total Education in Alcohol Management or Grocers Education Training Seminar programs for specific licensees.

The Training Officer is continuously engaged in training Commission state store personnel with an in-house program dealing with proper procedures for checking Ids and dealing with intoxicated patrons.

The Training Officer is entrusted with the data bases for all training conducted on behalf of retail licensees, Commission state store personnel, and documentation of the training requirements of investigators.

OBSERVATION NO. 7 (Continued)

When not actively engaged in these pursuits, the Training Officer works on responses to related correspondence and is occasionally utilized to help with updating licensing files or handling simultaneous multiple location licensing. **These are strictly secondary in nature and do not routinely take one to two days of the work week as reported by LBA.**

Observation No. 6 recommends the elimination of the administrative assistant chief's position and reallocating the resources toward another investigator. That same observation makes note that no person should supervise another of equal labor grade.

Observation Nos. 5 and 7 recommend the education and training officer return to the field and carry licensing and investigative case loads. The observation also recommends that assistant chiefs carry no case load and be responsible for "investigator orientation" (training) and responsible that subordinates meet training requirements.

This observation recommends that "a centralized SLC training officer will have the responsibility of coordinating training and education for investigators and other division personnel". This we assume includes creating and updating curriculums for Total Education in Alcohol Management, Grocers Education Training Seminar and state store education programs, creating manuals for both training and procedures, supervision of investigator, examiner and office staff training, licensee training, public and civic group presentations, and police agency training.

The labor grade for this new position would have to be at least LG 22 - using LBA's assessment that a person of equal labor grade should not supervise another of equal labor grade.

If the purpose of this position is to create, maintain, update and ensure adequate training/procedure manuals, track and certify investigator training requirements, create and maintain data bases, issue certificates of training and supervise training of all trainees, the position will need at least one person to actually do public, police, licensee and store education programs which train hundreds of persons annually. This person would have to have the requisite teaching/training experience and legal training to answer the questions which are associated with such programs.

We currently have an assistant chief at labor grade 21 who as a part of his duties currently oversees these functions with the aid of an education and training officer. The process is on going and will not be accomplished quickly, but has progressed at what we believe is a respectable pace and is slowly overcoming 50 years of neglect.

LBA recommends returning them to the field, yet at the same time, seemingly recreates the same positions in the form of a centralized training position. The Commission fails to see how this will actually provide any savings, but does see how it would cause greater expense in the times of austerity and budget cuts now being imposed by the executive.

OBSERVATION NO. 7 (Continued)

We do not believe that a single job specification can perform the varied duties required. Although this looks more orderly on an organizational chart, the reality is that all employees within the organization must have cross-training in tasks required to achieve the real goals and be flexible enough to adjust to changing situations and needs. The single purpose of a job description, although proper for classification purposes is not the direction we wish to follow.

We will review the Senior Investigator supplemental job requirements with our Chief of Enforcement to insure that this supplemental job description is correct. If any changes are made we will submit this to the Division of Personnel for review.

LBA REBUTTAL:

The agency's response contains statements that directly contradict those made in other responses. The senior investigator position is unnecessary.

OBSERVATION NO. 8

MARKET PLANNING PROCESS SHOULD BE IMPROVED

AUDITEE RESPONSE:

We concur, in part, with the observation of the Office of Legislative Budget Assistance Audit Division (LBA) with respect to the Marketing and Merchandising Plan annual updates.

It should be noted that the Commission's Marketing and Communications Plan, developed for Fiscal year 1993 through Fiscal Year 1995, represented the first time a comprehensive multi-year marketing document had been prepared by the Commission. The plan was developed with input from key Commission staff members and was ultimately circulated for comment among elected officials including: The Governor and Executive Council, Chairman of the House of Regulated Revenue Committee, as well as both the Speaker of the House and President of the Senate.

The LBA incorrectly states that there have been no revisions or updates to the original plan. In light of a dramatically changing competitive environment, numerous changes have been made and implemented since this three-year plan was originally written. Although these changes have not been memorialized in the form of a formal written addendum to the original planning document, it must be noted that over the past three years the Commission's marketing staff position was vacant twice.

It should also be noted that the Commission's Marketing staff, Purchasing, and Stores meet weekly to determine short term tactical planning.

The Commission concurs with the recommendation that formal annual updates be provided to any multi-year Marketing and Merchandising Plan.

Presently, the Commission has completed a three year business plan and it is anticipated that this document will be revised, as needed, on an annual basis. This business plan incorporates implementation programming which develops long term tactical strategies among other elements.

We agree that the MIS Division should be involved in the planning process of the Commission's Marketing Plan, and all directors had input into the current three-year plan.

As was reported to the LBA, the current three-year Marketing Plan was developed after careful review by the Commission, the marketing staff, and its advertising contractor. Several drafts of the plan were produced, with all directors receiving a copy of the plan for input prior to final adoption. Final copies were subsequently made available to directors with copies also forwarded to the Legislative leadership, Executive Council, and Governor.

OBSERVATION NO. 8 (Continued)

The completion and adoption of this plan by the Commission represented the first time a comprehensive three-year detail Marketing Plan has been produced. It established a more defined marketing and communications discipline which previously did not exist.

It should be noted that MIS data is available and has consistently been used on a weekly basis in analyzing past performances of all products at both the produce and unit level. Product sales selection and projections were developed from this data. MIS is very much involved in this process.

The MIS Division director, as well as all division directors, through regular weekly director meetings, had and continues to have an ongoing opportunity to provide input into not only the marketing planning process, but current day-to-day activities, as well.

The customer zip-code analysis, conducted by an outside contractor, has provided the Commission with perhaps the most comprehensive and actionable marketing research ever conducted by the Commission. It has proven crucial in understanding customer origin and buying patterns and has resulted in significant beneficial changes in our sales, marketing, and advertising strategy. At the time this analysis was originally conducted, it was determined that the MIS Division lacked the human resources and research expertise to conduct this study independently and in a timely manner. The MIS Division did work cooperatively with the subcontractor and provided critical assistance in a variety of areas.

This zip code analysis was a 12-month study which was completed in July of 1994. Now that a research protocol and benchmark has been established, the Commission anticipated the MIS Division will conduct all future zip code analysis.

Limiting the direct use of advertising funds to news print and radio is misleading and not what the market expenditure is actually designed for. More information will be forthcoming on this issue in responses to other observations which are the same as this or which may differ slightly.

We concur with the LBA that the developing, writing, and updating of the Marketing Plan should be the responsibility of marketing and sales-related personnel. As has been previously noted by both the Commission and the LBA, several personnel changes have occurred at the director level in marketing and stores divisions over the past several years. Naturally, this reality resulted in an inability to maintain consistent planning and decision making in these areas. Nevertheless, throughout this period of personnel changes, the Commission itself maintained regular weekly marketing meetings and continues to be directly involved in the all-important marketing and sales efforts.

OBSERVATION NO. 8 (Continued)

Both the marketing and director of store operations positions are now filled and these departments are under direct supervision and leadership, significant gains have been made in the short-and long-term planning process. Most recently, the development of the Commission's Business Plan included all directors with open channels of input from critical areas of the Commission's operations.

LBA REBUTTAL:

In our interview with the MIS director on January 13, 1994, he stated that he had no involvement in the plan's development, did not know what data sources are used for SLC market research (he guessed it was taken from vendors), never had any "discussion on how to implement the plan," and that the project manager "simply provided information the ad agency wanted."

OBSERVATION NO. 9

ADVERTISING BUDGET SHOULD BE REVIEWED

AUDITEE RESPONSE:

We concur, in part, with the observation of the Office of Legislative Budget Assistant Audit Division (LBA) with respect to review of the advertising budget.

We agree with the LBA that the Commission's advertising budget of just 0.29 of 1 percent of the gross revenues needs to be reviewed, given the highly competitive nature of the industry. The New Hampshire Liquor Commission's primary market area extends throughout New England. Secondary markets include New York and New Jersey, as well as parts of Canada. However, the Commission's advertising budget is not sufficient to effectively advertise throughout this area. In fact, because of the relative high media cost in many of these geographical regions, the Commission is forced to concentrate it's limited advertising media resources primarily in the Massachusetts market.

An increased advertising budget would allow the Commission to extend its advertising reach into outlying markets which are known to produce significant sales. As the spirit and wine industry becomes increasingly more competitive, it is imperative for the Commission to effectively communicate its value-orientated message.

The LBA's comment with respect to radio advertising as "relatively more expensive" than newspaper advertising is factually incorrect. Using the advertising industry standard of measurement of cost per thousand (cost to reach 1,000 people), the Commission's standard radio schedule has a cost-per-thousand of $5.63. This compared to a cost of $7.61 per thousand for the Commission's standard newspaper buy.

However, cost per thousand is only one of several considerations used in the media selection process. Restrictions on the type of broadcast advertising for spirits make comparisons of newspaper and radio solely on a cost basis highly inappropriate. The LBA's observation, in this regard, inaccurately misleads the reader to assume that the Commission favors a "relatively more expensive" advertising medium. Again, this is factually incorrect and reveals the LBA's knowledge in this area is superficial at best.

Again, the LBA's observation that the Commission has no "objective method to evaluate its advertising budget" is factually incorrect and also highly misleading.

In the spirit and wine industry there are a variety of methods to measure advertising effectiveness. Over the past several years, the Commission had adopted numerous quantifiable methods to measure the effectiveness of both its advertising and sales merchandising efforts.

OBSERVATION NO. 9 (Continued)

Key among the many methods of measuring advertising effectiveness is the sales analysis review. Following each sales period, the Commission reviews sales which compares data from previous promotional periods. The marketing staff analyzes the impact advertised sales have had on total product sales. This sales date is reviewed with the advertising contractor and adjustments are made as deemed warranted. The sales review is conducted for each Commission sale to provide direct and immediate analysis. While the review and analysis of sales data is used for a variety of purposes such as product trend review, financial impact, etc., it does provide an important and viable means to evaluate advertising. The fact that the Commission does not label this undertaking as a "formal advertising review" does not mean that this process does not exist. It should be noted that the LBA, while aware of the existence of weekly marketing meetings, did not choose to observe this process. Doing so would have revealed the Commission's ongoing process of advertising review, as well as providing valuable input into the complex issues involved in marketing spirits and wines within a control state context.

Other methods for advertising review include, but are not limited to the following.

<u>Newspaper Advertising Coupon Analysis</u>

Regular Commission advertising included discount coupons placed in a variety of newspapers. Consumer redemption rates are tabulated with a comprehensive analysis made of the effectiveness of the newspapers used. This procedure has resulted in the shifting of advertising to publications which have demonstrated the strongest ability to "pull" customers to New Hampshire State Liquor and Wine Outlet Stores.

<u>Direct Mail</u>

The Commission often uses direct mail solicitations to consumers in out-of-state markets to communicate special sales and products offers. Each promotion redemption rate is analyzed with a comprehensive review of total sales generated, average purchase amount, as well as the redemption rate by state and other categories. The Commission's success with direct mail redemptions is particularly noteworthy and has achieved redemption rates significantly in excess of industry standards.

<u>Monthly Sales Flyers Inserts</u>

Several times each year the Commission develops a special sales flyer which is inserted in select out-of-state newspapers. Unlike a newspaper advertisement, this flyer (commonly known as a circular), provides information on a variety of Commission products and sale offerings.

OBSERVATION NO. 9 (Continued)

Following each flyer insertion, the Commission reviews redemption rates and compares the sales results with changing offers. Again, the Commission has had significant success with this program, with redemption rates exceeding industry averages.

Naturally, like all industries, there are some forms of advertising used that do not lend themselves to direct quantifiable analysis. However, the majority of the Commission's advertising is evaluated, to the best extent possible, on an ongoing basis.

It is important to point out that the Commission's marketing and advertising efforts have received national acclaim for effectiveness and creativity. While additional resources could be dedicated to further researching advertising effectiveness, the Commission believes the current methods of measuring advertising effectiveness are consistent with generally accepted industry practices and in keeping with the priorities of a limited research budget.

The LBA continues to allege an absence of readily available data for researching the impact of advertising on sales and marketing performance, insufficient coordination between marketing, sales, and MIS, as well as direction from top SLC management. Rest assured that data coordination, and direction from the Commission, in fact exists. The SLC contribution of almost 1/2 billion dollars to the general fund within the audit period is proof positive and flies in the face of the LBA observations.

We concur with the LBA's observation that expenditures for research-related functions should be targeted for future budgeting. Regrettably, limited budgets have prevented the undertaking of research which would be useful in a variety of marketing and sales functions. Like all state agencies, the Commission must carefully review the benefits of this information against the added costs associated with obtaining it. The Commission has insisted that all research conducted be actionable and provide immediate bottom-line benefits to the mission of the agency.

LBA REBUTTAL:

The agency's response regarding the cost per thousand standard radio advertising does not take into consideration another factor, effective circulation, that should be assessed when comparing radio and print media expenditures. Effective circulation for newspaper advertising is circulation multiplied by "pass on readership," while radio impressions are counted by effective listenership. When pass on readership factors are greater than effective listenership, then radio advertising does become more expensive.

OBSERVATION NO. 9 (Continued)

The agency's use of coded coupons and direct mail were both relatively new at the time of our fieldwork. If the agency has been able to quantify and use these data to target its media expenditures that is an improvement that supports the type of review we recommend. We hope the agency is preserving accumulated data to use in an analysis of performance over time.

OBSERVATION NO. 10

STORE STAFFING SHOULD BE REVIEWED

AUDITEE RESPONSE:

The Commission concurs.

The Commission concurs that the Liquor Commission should review store staffing levels to determine if they are sufficient. Store Operations budgets have been cut severely. These cuts diminish the ability to provide proper customer service. Security and employee training have also suffered due to the budget reductions.

The Liquor Commission is unique compared to other state agencies in that it operates a retail business. Customer service is high priority and adequate staffing is essential to insure repeat business. Store budgets should be a reflection of sales and net profit generated by the stores. The Commission should be operated as an enterprize fund.

The Commission has been forced to close stores in the past to comply with budget restraints. Some of the business from these stores shifted to other NH stores but some of it was lost to neighboring states.

The Commission is forced to operate some small stores with one employee. For proper security a minimum of two employees should be available to operate the store and make bank deposits.

Reduced hours of operation in some locations would result in lower payroll expense but the revenue reduction from lost sales would out weigh the savings.

OBSERVATION NO. 11

SLC SHOULD ASSESS COSTS AND BENEFITS OF A ONE-WAREHOUSE OPERATION AND PUT LICENSE FOR PRIVATELY-OWNED WAREHOUSE OUT TO BID

AUDITEE RESPONSE:

The Commission concurs, in part, with the observation and recommendation. The Financial Management Director has provided cost/benefit analysis on the single warehouse concept on several occasions. A request has been made in each of the last two capital budgets for funds to expand the existing Concord warehouse. The requests have not made it through the governor's phase of the budget process even though they estimated a net profit of over $1 million. Options for expansion of the existing facility, purchase of an existing building and lease of an existing facility have been analyzed. The best opportunity came from a bankruptcy disposal, but fast action was required which is usually not possible in a government environment. The following options were submitted to the governor's office for consideration in December of 1992.

The commission had an opportunity to buy an existing 140,000 sq. ft. warehouse in Londonderry that would have met the operational needs of the commission. The first plan was based on the outright purchase of the property and the addition of 60,000 sq. ft. of warehouse space. The plan conservatively estimated additional annual bailment revenue at $2 million (the current private warehouse that this would replace generates $2.5 million), a savings of $342,000 from transportation efficiencies and annual savings of $191,131 in charges the state currently pays to the private warehouse. Additional savings would accrue to the state from reduced cycle times that would lower inventory carrying cost and decrease the state's investment in inventory by $2 million.

Additional operating expenses would cost the state approximately $752,000 annually. Amortization of the $5.9 million capital investment over 15 years @ 6% would cost the state $603,000. The net gain to the state's general fund was estimated at $1.4 million.

A second option was submitted based on a lease with a purchase option after 5 years. This option provided an annual net profit to the state of $1.2 million annually for the first five years. No action was taken on either plan.

The commission has considered a total private warehouse concept. Two major issues surfaced in this study. First, the commission would experience a $1.2 million revenue loss with a decrease in expenses of approximately $800,000. That would represent a $400,000 net loss to the state that would not be offset by a $200,000 savings in transportation cost. Secondly, the commission would lose control of this vital piece of the distribution channel. Current statistics show a much higher rate of stock-outs in the

OBSERVATION NO. 11 (Continued)

private warehouse than in the state warehouse. For this reason, the state warehouse handles as many high volume items as possible. In an era when customer service is vital to retaining market share, the commission doesn't want to be totally dependent on an external source.

The commission will continue to pursue the single warehouse concept. Each opportunity must be evaluated individually as location, cost of lease or purchase, occupancy cost, etc. all impact the bottom line. The commission will make further recommendations on this issue in FY '96.

The Commission has tried for the past 24 months to develop with the Attorney General's Office an RFP (bid) process to utilize the privately-owned warehouse meeting SLC requirements at the lowest cost possible to private vendors. We have been working together with the Division of Purchase and Property and the Attorney General's Office in order to develop this RFP. The RFP will be ready to go out in the 4th quarter of Fiscal '96. We hope to maximize our license fee at that time to increase revenue to the state consistent with what the market will bear.

OBSERVATION NO. 12

SAFETY FACTORS ACCOUNT FOR THE MAJORITY OF WORKERS' COMPENSATION CLAIMS IN THE SLC WAREHOUSE

AUDITEE RESPONSE:

The Commission agrees in part with the observation and recommendation. We agree that the lighting in the warehouse is poor, ventilation could be better and the warehouse is undersized which leads to unsafely stacked cases. We would also like to point out that the racks are too small to allow for proper lifting and the equipment is very old making it difficult to purchase parts for proper repair. We have unsuccessfully requested funding for a new warehouse or warehouse addition, new lighting, new forklifts and racking in the pick area during the budget process on numerous occasions.

The issue with unauthorized smoking has been resolved with the inception of the commission's smoking policy. The forklifts have been on a preventative maintenance agreement for the past 18 months and we've seen a marked improvement over our previous situation where we used in-house staff for maintenance.

The Commission did investigate the use of abdominal belts (this is the proper terminology, not back brace, lifting belt or back belt) through several sources including the Workers' Compensation Commission for State Employees, Risk Management, New Hampshire Center for Back Care at Concord Hospital and Lewis Products, a distributor of Valeo back support products.

The consensus was that there is little concrete evidence that abdominal belts prevent back injuries and many doctors feel that long-term use may be detrimental. The State's Workers' Compensation Commission for State Employees cautioned us against mandating the use of belts. We asked concerned employees to obtain a recommendation from their doctor on a case by case basis as each employees' needs are different. None of our employees were able to get a doctor's recommendation. Concern exists for the state's liability should we purchase belts and they are subsequently found to cause injury to an employee. As always, employees are free to purchase their own belts and wear them at work.

Current data suggest that engineering solutions offer the most effective means to reduce injuries in the work place. The technology is available but would require a considerable investment by the state. Prior budgetary requests for this type of investment have died early in the budgetary process.

Administrative Controls provide the next best solution. They include training, job rotation, job enlargement, job method changes, employee selection and light duty. Unlike reengineering, Administrative Controls are temporary in nature. The NSLC has had preliminary discussion with Helmsman Management Services, Inc., the state's new w/c administrator. In the coming

OBSERVATION NO. 12 (Continued)

months we will be looking at both engineering and administrative control solutions with the Risk Management Division of Helmsman. We will address all issues raised in this observation including safe equipment operation training and the development and implementation of a formal safety program.

Continuous education provides the third best solution. The Commission did hire the New Hampshire Back Clinic at Concord Hospital to video tape the warehouse work process and make specific recommendations to workers on how to prevent back injuries. The video was reviewed with employees and proper lifting techniques were demonstrated. Helmsman will provide another back clinic to warehouse employees on 12-APR-95.

The two most effective ways to reduce workers' compensation claims are prevention and claims management. The Commission will continue to use available resources to pursue the most effective prevention alternatives. We have been in contact with Risk Management requesting help with a safety review and re-engineering. Claims management could have a significant impact on workers' compensation cost. Risk Management told us that they recognize the benefits of claims management and look forward to working with the new management consultants at Helmsman.

OBSERVATION NO. 13

ANALYTICAL CAPABILITIES FOR MARKETING AND SALES FUNCTION SHOULD BE IMPROVED

AUDITEE RESPONSE:

We concur, in part, with the observation of the Office of Legislative Budget Assistant's Audit Division (LBA) with respect to Observation No. 13, Analytical Capabilities for Marketing & Sales.

The current trend of relying on "sophisticated PC-based analytical software" to be a panacea with standard formulas is, in our opinion, not always the best method.

The competitive sales environment is one of constant fluidity which requires different formulas or strategies for each product and category.

There is no substitution for human, data driven and flexible sales analysis and forecasting. We currently utilize data such as past sales history at certain price points and profit levels while taking into account environmental factors such as time of year, weather, applicability of product to holiday period and the competitive environment. To re-program the software to account for these constant changes takes more time and is less accurate.

There has always been available to Marketing and to the Commission, a spread sheet analysis taking into account the necessary sales data regarding sales projections and ultimate sales performance. More recently, the Marketing Director has upgraded this analysis to include necessary logical steps to properly select products for the maximization of sales. This was done at no additional cost to the Commission.

In regard to research, the audit has mentioned the customer origination or "zip code" survey. It neglected to mention data collected from the American Express coupon program and several other coupon tracking programs run during the year. We are always searching for economical methods to gather pertinent research data.

The installation of a new computer system will allow us sufficient capability to adapt to necessary forecasting and research requirements. However, significant resistance to the zip code survey was experienced from customers who viewed it as an invasion of privacy. After 12 months, the store operations division, reacting to customer complaints, lobbied for discontinuing the program.

Market research is also expensive. We currently have a program on the drawing board to define, segment and target mid-fine wine customers which is "on hold" due to budgetary problems. The current budgetary environment suggests that we will have less money available for research projects in the future.

OBSERVATION NO. 13 (Continued)

The audit states that "sales forecasting is key to maximizing in-store product availability with minimal inventory investment". We agree. Sales forecasting and projections are in fact included on a spread sheet program and are significant factors in choosing products for sale and advising purchasing on how to handle inventories. Price competition, type of advertising, costs are all factored into the equation. We do not, at this time, have the ability to segment via customer type.

As outlined above, the SLC does have, and has always had, sufficient data readily available and does make constant use of it. Just because it is not formalized in a PC based software package does not mean data is not used or that is not effective. The LBA audit observation that such data is absent is incorrect.

Also, the audit comments that the SLC performs rudimentary ad tracking. The process may seem basic, but it is very accurate, complete and useful. Last year, 43% of all spirit sales nationally came from 25 brands. In that regard, all print ads from competition are monitored for these brands that comprise such a significant part of our business. The SLC does not have the budget or manpower to track hundreds of brands nor is it necessarily based on volume.

The audit states that research and evaluation should be conducted in house for maximum control. We believe this research can be done more efficiently and economically by an outside firm. Also using outside sources allows for different ideas and opinions developed by people who have a more specialized expertise in research. Final control over the purpose and the process certainly remains at the SLC.

We continue not to concur with the observation that there is insufficient coordination between Marketing and sales functions and the MIS Director for planning purposes and particularly do not concur that there is insufficient MIS-planning, supervision, and direction from top State Liquor Commission management.

The Commission does give very specific direction to all divisions within the Agency and directs and develops coordination efforts through team assignments on specific problems and projects as well reporting requirements directly to the Commission. A single Commissioner is assigned to each division as a liaison as well as a facilitator to assist and ensure that thorough recommendations reach the full Commission and are acted upon as required. Also weekly meetings with staff directors are held to further discuss problems, ideas, coordination of efforts, and procedural recommendations on a team effort basis.

OBSERVATION NO. 14

MIS SUPPORT FOR STORES SHOULD BE IMPROVED

AUDITEE RESPONSE:

The Commission agrees in part with the observation.

The MIS department has been working on improving its use of in-store equipment but has faced problems for months in interfacing with the Nixdorf equipment. Higher priority projects with greater payback have also commanded the time and attention of MIS staff.

However, we are currently awaiting a technical solution from Nixdorf with alternative connections between store and headquarters. There are ways to use E-mail right now, but we have not initiated them because they are not yet use-friendly enough to obviate the need for user training. We are not able to budget for any additional training at this time. However, we anticipate a technological solution in early 1995 that will allow us to better leverage our in-store processors for communication purposes.

In the meantime, the issue of ample notice of upcoming sales to store personnel is being addressed on a couple of fronts. First, our new Director of Marketing has cleared up much of the backlog that existed by virtue of that position being unoccupied for approximately six months before his arrival. He is now working ahead on sales and has an "inventory" of information to send out to the stores with longer lead time than during the LBA audit period. Secondly, the Wine Marketing Specialist and the Directors of Purchasing, Store Operations and Marketing have worked out a system to address bailment stock-out which may have exacerbated the problem at the store level.

However, it must be noted that the fliers, posters and other promotional support materials that play such an important part of in-store merchandising efforts must be physically delivered, cannot be simply electronically communicated. Our greater ability to anticipate sales and centrally prepare these point of sale materials will take care of most concerns by store personnel. Furthermore, the Commission reserves the right to make last minute changes, additions and omissions, as market conditions warrant. For example, if a distiller, winery or broker offers us a very good deal on short notice, we're not going to pass it up just because store personnel find it inconvenient to implement it quickly. Most of our better store managers understand that is part of their responsibility to react quickly when it is in the best interests of the business to do so. There are other scenarios where their quick cooperation is mandatory -- and there always will be.

Regarding the issue of inventory shrinkage, it's important to note two reasons why we disagree with both the observation and the recommendation. The computer reports that are prepared are tools for internal use only. The equation for normalized losses by store is well known to the Director of

OBSERVATION NO. 14 (Continued)

MIS, but it is not necessary to reiterate it to everyone when the report is produced quarterly. It is a useful "red flag" report with actionable data. If further analysis is needed, the swing report by SKU (product by product, by store) can uncover useful information only when an investigation is warranted.

Most importantly, however, is that fact that investing much more time or effort in inventory shrinkage would clearly be misallocated. The attached memo benchmarks the SLC as unusually effective at inventory security. Over the audit period, the SLC's losses average approximately .044% of gross annual sales. Losses for all retail businesses are nearly 5 times as much, and for the liquor/beer/wine category of stores, it's over 3 times as much as the SLC's losses. Anyone with "real world" business experience would recognize the LBA's recommendation to design additional reports as an example of increasing investment resulting in substantially diminished returns.

LBA REBUTTAL:

The agency's response regarding the impact of training personnel to use the E-mail system appears to contradict the response to Recommendation NO. 4, where the agency stated the supervisors "help train their area stores on the new registers and computer systems." Training for the E-mail system should be from supervisors to managers and cashiers.

Neither our observation nor our recommendation suggest the agency should pass up promotional opportunities, even short term ones. We recommend finding ways to provide more timely information to stores regarding promotions.

We agree that inventory shrinkage levels may not warrant much more investment for developing additional reports. As an interim step the agency should at least develop and use exception reporting for inventory management. Exception reports would be a time saver because only those stores exceeding management-set parameters would receive scrutiny. Over the long term the agency could develop additional analytical reports.

Measuring shrinkage levels across an entire enterprise can be misleading as individual store variances often cancel each other out enterprise-wide. Critical to an automated replenishment system is store inventory accuracy. Without a high degree of accuracy, an issue which we address in other observations, the automated replenishment system can be compromised to the effect that stores receive more or less replenishment than warranted, translating into lost sales and overstocks. Inventory management becomes more critical as the agency moves towards more automation with its shelf management system.

OBSERVATION NO. 15

ACCOUNTING SOFTWARE NEEDS UPGRADING

AUDITEE RESPONSE:

The Commission concurs with the observation and recommendation. The Financial Management Director and the Chief Accountant have worked with MIS and Office of Information Technology to develop a solution to this problem. The commission made this item a top priority in commission's recently revised business plan. Accounting and MIS presented their proposal to the Office of Information Technology in mid October and received approval for a major upgrade of the current system. The Commission will be submitting a five year approval in November 1994. The contract covers the purchase and maintenance of new software for General Ledger, Accounts Payable, Accounts Receivable and fixed assets. Included is a module for enhanced reporting capabilities. Training and installation are scheduled for December, January and February with the total project completed by March 1995.

OBSERVATION NO. 16

IN-SERVICE TRAINING IMPROVEMENTS NEEDED

AUDITEE RESPONSE:

Enforcement Division Personnel

A. **We concur in part.** LBA auditors are correct in their assessment of the completeness and retention of records for five years. For the years prior to 1990 records are, in fact, sometimes incomplete or the curriculum and attendance poorly substantiated.

Part of the reason for the lack of good documentation of the various subjects taught in our in-service training was as a result of a misunderstanding when the word "outline" of what is taught was used, the Education Officer believed they meant a skeleton outline as to what would be taught, while in reality Police Standards and Training was trying to convey that it was necessary to fully outline the subject matter/content taught. This erroneous concept was questioned, by the Administrative Assistant Chief - because of the apparent simplicity - when he took over as the Education Officer's supervisor. He was told by the Education and Training Officer that only a simple outline of what was covered, a competent instructor and a signature sheet would meet the requirements for Pol 403.01.

The Enforcement Division has taken steps to implement a new format for documentation of in-service training based upon a model supplied by Police Standards & Training. This format should eliminate future problems.

B. **We do not concur in part.** Paragraph 1: Liquor Investigators do receive adequate and relevant amounts of training in accordance with Pol 403.01. The Commission's Enforcement Division contacted Police Standards and Training after receiving this memo and ascertained that Pol 403.01 is written broadly to give agencies wide latitude as to what training is deemed appropriate.

Pre- or post-approval by the Police Standards and Training Council is not required for departmental in-service training required by Pol 403.01.

C. **We do not concur that one officer was short eight hours in training in 1989.**

1. According to the Enforcement Division records Inv. O. received in-service training on November 29, 1989 (6 hrs) Total Education in Alcohol Management and - undocumented on December 28, 1989 (2 hrs) "B" Team/TAP, for a total of 8 hours in-service training.

OBSERVATION NO. 16 (Continued)

Enforcement Division Personnel (Continued)

D. **We concur that one officer was short 2 hours of training in 1991.**

E. **We concur that two officers were short 2 hours of training in 1992.**

F. **We do not concur that the Chief of Enforcement willfully violated Pol 403.01.**

The Liquor Commission unquestionably believes, the Education and Training Officer, and the Chief in particular, in no way "willfully" violated Pol 403.01 when making that certification, nor would they have compromised the agency had they been aware of the discrepancy. This is evidenced by the fact that in 1990 the Education and Training Officer documented in a memo that 3 investigators needed additional training to meet the requirements of Pol 403.01 and subsequently scheduled the 3 for courses to meet the training mandate.

It should also be noted that complete records were maintained for the years 1987, 1988 and 1993, which demonstrates that the agency was making the effort to be in compliance at all times.

Training for Store Employees

The Commission concurs in part and does not concur in part.

The Commission concurs in part that there is a significant need for more training in the Store Operations Division. The stores Division of the NHSLC has operated with the same expenses for the last five years (graph attached). During this time sales have increased, heat and utilities and all other operating costs have increased. The current budget allows for register staffing, customer service, and maintenance of stores. When employees leave their assigned work area for training purposes, someone must cover that area and often travel expenses are incurred. Training of employees has become more difficult to accomplish but still continues. The joint training venture with the University of New Hampshire was discontinued because of budget restrictions. Training is now provided by each employee's immediate superior and continues daily at each of the sixty-eight store sites.

The Department of Personnel is offering a management training program which is scheduled to being in early 1995. This program will be mandatory for all members of the NHSLC management team. The Directors of Marketing and Stores have designed a comprehensive product training program which will also begin in January 1995. This program will be administered in each area, after the initial train the trainer training is provided at the Concord headquarters. Additionally, product information sheets are now required for each item stocked and notebooks containing this information will be at each location for training and review by all employees.

OBSERVATION NO. 16 (Continued)

Training for Store Employees (Continued)

Currently the Director of Stores and the Personnel Coordinator are attending regional meeting and conducting training seminars on Sexual Harassment, how to handle a bomb threat and store presentation.

The Commission does not Concur regarding training in the areas of sales to minors and inebriates. The Commission provided training to all store personnel in the fall of 1992-from September through December-which was conducted by Sr. Investigator L., the Education and Training Officer of the Liquor Commission. He visited all stores teaching a program for proper ID checking and how to determine if a person should not be sold product due to intoxication. The program was taken on the road and the classes were conducted all over the state, all SLC employees were trained including Store Managers.

Currently the Commission is engaged in similar educational training conducted by Sr. Investigator P. which covers proper ID checking and how to determine if a person should not be sold product because of intoxication. This program has not been completed through-out the entire State and now continues, to offer training to seasonal and temporary employees in the evening to those not available during the day.

To provide continuous training we are currently in the planning stages of creating two separate training videos. One to cover ID's and sales to minors and one to update the training modules that were developed in conjunction with UNH. The end result would be that the videos will be available at each store for existing employees to review and for new employees to view as they being their training.

The Commission does not concur that the lack of training in wines means some SLC store managers do not order premium wines that are in demand. The selection of wines offered at each store is the decision of the wine marketing specialist. The offering is based on the wine specialist's analysis of the sales history developed by all stores. The Store Manager may add to this list if customers request products not offered, but the wine specialist must approve all such requests.

This Commission recognizes the importance of providing continuous training to all employees. Today's skyrocketing expenses has forced even the most successful retailers to administer most training at each individual store. The Store Manager is responsible for the success of the store and a well trained organization is vital to that success. Resources are limited, however, this Commission is dedicated to maintaining a well trained and informed organization and will continue to actively and aggressively improve our current training program.

OBSERVATION NO. 16 (Continued)

Training for Store Employees (Continued)

Several possible training programs were studied before committing to our current approach. This Commission is committed to training; however, funding is limited.

The program consists of training 3 to 4 employees from six strategic areas throughout the State. The employees selected will attend six, three hour Train the Trainer sessions here in Concord. Each session will be video taped for future use in the field. When complete, the Trainers will return to their areas and conduct product training for all other employees. All area sessions are to be conducted on Tuesday mornings with classes of not more than twelve.

The initial Train the Trainer program is estimated to cost $4,176.00 replacement personnel and travel costing $1,019.00 for an estimated total of $5,195.00. Store Operation's class 50 funds have been very closely monitored resulting in available funds for this important program.

The program is scheduled to begin on April 4, 1995.

Financial Management Training

The Commission doesn't concur with the observation or recommendation. The Financial Management Director has made training a priority. The financial management division currently has 16 employees. They have attended over 90 professional development courses since the current division director was appointed in July '91. Considering some of these employees are new, internal training on issues like sexual harassment aren't included and the numbers don't include training received by employees who no longer work in the department, we believe this evidences a strong commitment to training. On average each employee has participated in two courses per year during the past three years.

The cross-training issue is due to high turn-over and low wages more than it is due to a lack of support for cross-training. An example of this would be in cross-training for credit card processing. The current director, recognizing that cross-training in this key function didn't exist, requested that the accounts receivable supervisor oversee the cross-training of this process. The first person to be trained left the division for an internal promotion shortly after training was complete. The second person to be cross-trained also left the unit for a promotion within the division. The third person trained left for an external position that provided appropriate compensation. Currently, the position is vacant and the only back-up for this function is from the general ledger supervisor (who has given her 2 week notice -she's leaving for a better paying external position) and the Chief Accountant.

OBSERVATION NO. 16 (Continued)

Financial Management Training (Continued)

We should clarify that the MIS department really doesn't "maintain" the accounting system. Historically, the system was maintained under a software support agreement with Computer Associates. During the budget cuts of the late 80's, funding for this support was eliminated. The MIS department doesn't have any qualified technicians with the expertise to support this system. We have requested funds in the '96/97 biennial budget to restore software support. Until that time the majority of the expertise that keeps the system running comes from the accounting department.

Each unit supervisor is responsible for cross-training in their area. Each area is backed up by the unit supervisor, general ledger supervisor and the Chief Accountant. As mentioned in several other observation responses, the weak point is in accounts receivable. The issue in accounts receivable will be resolved once the new supervisor is in place and completes training.

Cross-training is an ongoing process due to the never ending changes in personnel and operating procedures. The Commission and the finance director will continue to make cross-training and professional development a high priority when planning the use of available resources.

The issue of training is an important function of any organization and an integral part of employee development. Unfortunately the extent of training is subject to funding available through the budgetary process. Once again we are being asked to reduce the present budget and the next two year budget.

At present, we utilize the Division of Personnel Bureau of Education and Training Program to allow our employees to sign up for specific courses which they feel will enhance their job skills. This is an excellent program and offers many courses designed to improve employee skills.

Our Human Resources Administrator is working with the Division of Personnel as part of a joint committee to set up a training program to develop skills, knowledge and abilities to supervisory and management personnel in NH State Government. A recent survey was sent out to employees as part of a needs assessment program to develop this training.

Our assessment of the current training within our agency is as follows:

1. Enforcement Division: Mandated courses through Police Standards and Training. We feel this is an extensive program directly related to the job skills.

This is also answered under other observations. We should perhaps increase some training for accounting and clerical personnel under the programs offered by the Division of Personnel.

OBSERVATION NO. 16 (Continued)

2. <u>Financial Division</u>: We have utilized the Division of Personnel Program sending many employees to specific courses. We have also had in-house training on Word Perfect and Mapper training. Specifics are being addressed under another observation.

3. <u>MIS and Data Division</u>: Since this is a technical skill field, most employees within this division have specific technical skills which are job related skills and additional training in these skills is extremely difficult to set up any general training. Seminars put on by outside seminars must be evaluated as a viable option.

4. <u>Warehouse Division</u>: Other than one Back Injury Prevention class we have not had any other formalized training. Office Personnel should be able to utilize the Division of Personnel Programs offered. All other warehouse personnel should receive On the Job Training in operation of equipment and training time should be set aside to cross-train employees during the non-peak periods. This is also addressed under another observation.

5. <u>Marketing Division</u>: This division has received training in Mapper computer and Word Perfect and should utilize the Division of Personnel Programs courses for specific job skill training.

All the above mentioned divisions should be able to conduct some training for all employees under the present budget since all training can be coordinated and conducted in the Concord area without any great impact on work load or budget if it is scheduled properly. The present program offered under the Division of Personnel is a cost effective way to implement training within our agency, in most areas. If the proposed skill training for supervisory and management training programs is implemented this will be a valued added program in an area that is much needed for all state employees.

The State of New Hampshire under the Division of Personnel has a Bureau of Training which should be utilized by all state agencies to coincide with their own training programs. The courses offered are more than adequate for most cost effective training and utilizing existing sources available to implement a good training program. Since we contribute funds toward the Division of Personnel this appears to be the most cost effective way to train our employees and stay within our allocated budgets.

6. <u>Store Operations</u>: We fully concur with the observation made that we need training for our personnel at the store level. The two factors we need to consider are how to conduct the training needed and how we can fund this training under present budgets. Unlike other divisions which are geographically located in Concord and direct proximity to training sites available. The stores personnel are geographically scattered throughout the state which requires funds to pull employees out of the stores.

OBSERVATION NO. 16 (Continued)

The Division of Personnel Program on skill training for supervisory and management personnel, if implemented, will be the necessary program we need for our supervisory and management personnel and will fill the necessary void in our needs assessment program.

There is on going training for our store personnel on ID training and selling to persons of legal age, this is being conducted by our Enforcement Division.

We are also planning to train our store personnel on wine knowledge and customer courtesy, a program that is being worked on with the Director of Store Operations and Director of Marketing.

We plan to do this training in the very near future. At present, we plan to conduct such training during the months of January through April 1995.

The Director of Store Operations and the Human Resources Administrator will be working on a training program for store personnel that will be handled through the Store Supervisor/Manager on a regional level that will encompass job related specific training as well as supervisory skill training.

All training records should be maintained by current Directors who are responsible to implement training within their divisions. They should also forward copies to our Human resources Administrator to place in the employees personnel folder. We concur with your recommendation that a training coordinator should be established but do not concur that this is practicable under existing resources. We expect training to be the function of the Directors of each Division with some assistance from our Human Resources Administrator, if necessary. Under our present budget we plan to work on a training program that can be effectively implemented and perhaps we may be able to have one person coordinate this effort in the near future. At present we will coordinate a group effort to implement some training programs within the agency.

LBA REBUTTAL:

Enforcement Division Personnel

Despite this response and as subsequent events have demonstrated, the SLC did not provide LBA auditors with all the documents necessary to prove compliance with training requirements. Not withstanding the SLC's transmission of additional information, we still find inadequate documentation to demonstrate that all liquor investigators received the required eight hours of training each year during the audit period.

OBSERVATION NO. 16 (Continued)

Enforcement Division Personnel (Continued)

We do not state that the chief of enforcement "willfully" violated the rules. The observation remains that the SLC, intentionally or not, incorrectly certified its compliance with in-service training requirements to the Police Standards and Training Council.

Training for Store Employees

The store supervisor/managers and managers who actually supervise store employees reported to us the need for increased training in the area of sales to minors and inebriates.

The wine specialist reported to us that although managers have the ability to order and put an "absolute" for wine products into their stores, he must perform all wine-related management for some managers who have poor wine programs. Additionally, if customers desire understocked or non-stocked wine products, the SLC loses wine sales.

Financial Management Training

When requested the financial management director was unable to provide the LBA with any supporting documentation certifying financial division employee attendance at development courses. Furthermore, we reassert that <u>all supervisory accounting personnel interviewed</u> stated training, especially cross-training, needed to be improved.

OBSERVATION NO. 17

SLC EMPLOYEES ARE NOT EVALUATED ANNUALLY AS REQUIRED

AUDITEE RESPONSE:

We concur that we are not in compliance with RSA 21-I:42 (XIII)(a-c) regarding annual performance evaluations.

However, within the limits created by personnel rules and the union environment, we faithfully do "exception" evaluations. For example, despite the fact that we are not allowed to give bonuses or extra compensation for extraordinary effort or performance, we do give recognition at an awards ceremony and an occasional letter of thanks for a job well done. On the other end of the spectrum, we rule on letters of warning when someone's performance falls beneath the norms. This is an efficient way of establishing appropriate parameters for our employees, but does not conform to the need to produce a lot of paperwork to conform with law.

Despite the fact that performance appraisals are no longer held in high esteem by management experts (because they are inefficient and ineffective), we have instructed our Human Resource Administrator to send performance appraisals to all department heads on employees who have not been evaluated in calendar year 1993 and to report back to us no later than August 31, 1994 on compliance or non-compliance.

In order to provide administrative assistance to his office to accomplish this as an on-going process, we will need an additional full-time employee and will submit the request in the next budget cycle.

LBA REBUTTAL:

State statute and Division of Personnel administrative rules require that executive agencies perform annual personnel evaluations of all full-time classified employees prior to granting merit increases.

We do not agree that additional full-time assistance is required to ensure personnel evaluations are completed on an ongoing and timely basis.

OBSERVATION NO. 18

EMPLOYEES WORKING OUTSIDE OF OWN DIVISION WITHOUT DIVISION OF PERSONNEL APPROVAL

AUDITEE RESPONSE:

We concur in part with the analysis of Commission employees working outside of their own division in a way that may not be in strict conformance with the rules of the Division of Personnel Approval. We will address each of the three cases in turn.

1. The Commission does not concur with the observation or recommendation relative to the Administrative Assistant being shared by Financial Management and MIS. This position, along with a Clerk II, report to the Administrative Secretary in the Financial Management Division. The Administrative Secretary is responsible for compiling and reviewing forms, reports and data, schedules work assignments for subordinate office staff, performs shorthand, typing, filing, answers telephones, word processing and schedules appointments for two departmental directors, and supervises the mail room. The Word Processor Operator supports the goals and objectives of the Administrative Secretary by answering telephones, typing, word processing and filing. It is also within the scope of that position to train personnel on word processing software. This position also fills in for Financial Management Division employees when they are out on annual or sick leave.

The Commission believes that the present duties of this position are consistent with the supplemental job description and class specification, and that it is in the organization's best interest for this position to remain under the supervision of the Administrative Secretary in the Financial Management Division.

Our Human Resources Administrator has advised this employee to submit a position review request if she feels her duties have changed.

2. The Store Supervisor/Manager working on the Shelfman Project (a computer model for shelf space allocation to maximize profitability) still works for the Director of Stores. Just because the computer is his primary tool at this point in the project does not mean that the implementation of the plan won't have the most impact on Store Operations. This is a "temporary" assignment in the sense that at some point it will be completed (During May 1995).

As the Shelfman Project reaches its second phase, the person assigned to do it will spend less time at a terminal and more time in the stores, first in one store as a pilot project, and then in others as the roll-out continues. Failure to allow this to happen will jeopardize tens of thousands of dollars already invested, decrease future profitability, and overlook the unique combination of talents that the person assigned brings to the job.

OBSERVATION NO. 18 (Continued)

We will instruct our Human Resources Administrator to set up a meeting with the Director of Personnel to explore the expansion of current job descriptions to allow us to make the class specifications more flexible to meet the needs and goals of our Store Operations. If this is not possible under current administrative rules, we will complete the task on the track it's on now.

Once the shelf management is set up, we are convinced all Store Supervisors and Store Managers will be directly involved in its implementation and be a part of their responsibilities to monitor and maintain. Having someone with similar experience leading the project will be invaluable in assuring its success.

We do not concur that this position is working outside of the Stores Division.

3. We concur that the Supervisor/Manager working as the assistant to the Director of Stores is not on a temporary assignment. We also concur with your recommendation to submit the supplemental job description to the Director of Personnel for review and determination.

The tasks that this person is responsible for are absolutely essential to the management of Store Operations. A substantial portion of all Commission personnel report directly or indirectly to the Director of Stores. It would be unheard of in the private sector for someone whose span of control is approximately 900 people (presently 210 full-time and 681 part-timers) to have no staff support. There are special projects which need someone's undivided attention, analytical work, and miscellaneous trouble-shooting which require the focus of a responsible long-term employee. The person who is in the job now acted as our Director of Stores in the months between the retirement of our last one and the hiring of our present Director. He is an invaluable member of our team, and it is in the best interests of the Commission that he be permanently in the job that is now designated as "temporary".

We have submitted a supplemental job description.

LBA REBUTTAL:

As an executive agency, the SLC is required to comply with administrative rules promulgated by the Division of Personnel.

Notwithstanding the agency's argument, the store supervisor/manager involved in the shelf management project is working outside of his normal job description.

The SLC has incorrectly applied the concept of "span of control." The stores director's true span of control is limited to the supervisor/ managers.

OBSERVATION NO. 19

SLC SHOULD ANALYZE THE EFFECTIVENESS OF A TWO-YEAR RENEWAL CYCLE FOR MOST LIQUOR LICENSES

AUDITEE RESPONSE:

We concur. The Liquor Commission has been tracking developments in Pennsylvania where 2 year renewal cycles have been implemented. This experiment started some time ago and is only now being implemented on a state-wide basis.

We have looked at some of the positive aspects:

1. Less time spent on renewal licensing - more time for enforcement.

2. Could contain a 2nd year billing cycle to cut initial high cost to the licensee.

3. The licensee may appreciate less paperwork.

4. Less printing/filing/administrative cost to agency.

There are also negative aspects as well:

1. It is already difficult to keep license application updated as required by RSA 178:24, IX. A period of two years for a thorough review would probably result in greater problems documenting changes than we do now when it is checked, at least, annually.

2. An investigator spending more time on enforcing drunks, minors and after hours is less likely to ask questions about whether there have been changes to the premise or application documentation since the last visit.

3. The change would require extensive programming in MIS and testing of the system prior to the implementation.

4. Licensees would be paying double fees not knowing whether they would use the time, unless a 2nd year billing was developed and/or a refund policy instituted.

5. Vendor's licenses where fees are based on quantity sold would have to still be done annually or a special 2nd year re-cost to insure the state or the licensee was not unjustly treated.

OBSERVATION NO. 19 (Continued)

6. If 2nd year billing were developed, a greater possibility of delinquent renewal would result due to mail actually being lost or claims to that effect. Currently we deliver application and have a responsible party sign that they have received them.

In any case, the Liquor Commission prior to LBA's audit and this suggestion had been tracking the status in Pennsylvania and exploring the possibilities in this regard. More time must be spent to study the results of Pennsylvania and create our own plan, if conditions warrant after study, before any action is taken.

OBSERVATION NO. 20

MATERIAL SUPPORT FOR HOME OFFICES OF LIQUOR INVESTIGATORS SHOULD BE INCREASED

AUDITEE RESPONSE:

We concur in part the SLC should provide in-home office telephone lines to investigators who request them for SLC-business related calls as well as providing telephone answering machines for incoming calls after office hours. We additionally concur that post office boxes should be provided investigators.

To facilitate communications, the Commission has already installed an 800 number for investigators to call into the office, approved post office box reimbursement and authorized voice mail for each investigator. The voice mail and P O box reimbursement should be implemented by May 1, 1995. Future editions of the law books will carry the P. O. Box addresses and voice mail telephone numbers instead of the current street address and personal phone numbers of each investigator.

Investigators, unlike State Police and Fish and Game do not have people cover during off hours or days off and do not have direct office dispatch where a licensee can call in to have an investigator dispatched. They make appointments and keep office hours, albeit at their residence, similar to regular police detectives who are available through their police department phone. Instead of a secretary answering for them they take their calls direct on their work days and provide firsthand, prompt service to the licensee they directly service. Any other system would waste time, create the possibility of garbled messages and provide poorer service to the customer (licensee). Direct communication is always better than indirect and immediate response is always better than delay.

Prior to the LBA audit the issues have come up many times in prior years. Prior Commissions or administrations had not considered the proposals, either due to lack of available funds or the of perception that the needs were real. This year the Commission has agreed to follow through on the above issues, providing funding is available. (These have been requested in the 96-97 budget.)

We do not concur in part with the erroneous conclusion that LBA arrived at, namely that the Commission does not reimburse for necessary out of pocket expenses. Investigators have always been able to submit the in-state travel/expense forms for any items not routinely supplied by the office through purchase and property, which are needed for their work such as computer/typewriter ribbons, postage, related office items or expenses incurred while procuring evidence in criminal or administrative cases.

OBSERVATION NO. 20 (Continued)

Many investigators do not choose to retain and submit the necessary paperwork to collect a reimbursement, while others take advantage of tax advantages the IRS allows for expenses or the in-home office deduction. In any case, investigators can be reimbursed for necessary out of pocket expenses, provided they utilize available avenues.

Investigators, like state police and other state employees working out of their homes furnish desks (which may be as simple as using their kitchen table), file cabinets (which may be old liquor boxes), and a typewriter/word processor or computer (which is as complex or expensive as the individual believes they need to accomplish their job.

OBSERVATION NO. 21

ADVERTISING CONTRACT USED FOR NON-ADVERTISING PURPOSES

AUDITEE RESPONSE:

We do not concur with the observation of the Legislative Budget Assistant Audit Division (LBA) with respect to the advertising contract used for non-advertising purposes.

The Commission strongly disagrees with the LBA's interpretation of the contractual intent with respect to the word "advertising". Further, we would point out that the advertising appropriation is within the Marketing and Merchandising PAU and as such is designed to be all inclusive for those functions as they may relate to enhancing sales strategies and increased profitability.

It is our view that the word "advertising", as it appears in the advertising contractors contract, is intended to refer to the overall activities generally associated with the contemporary means of the marketing of spirits and wines. In fact, "Exhibit A" in the advertising contract, which outlines the scope of services provided under the contract, refers to a much broader concept of "advertising matters".

It is our view that this term, while ambiguous, refers not only to media advertising in the strictest sense of the word, but also includes related activities within the discipline of marketing, such as advertising research, direct mail campaigns, merchandising programs, sales promotional activities and, in this case, the shelf management program.

Certainly, had the Commission believed the use of the term "advertising" would be interpreted in the sense to limit activities solely to media advertising, it would have selected far different language for inclusion in this contract.

Using the LBA's narrow definition and interpretation of the word "advertising" would prevent the Commission from initiating customer information flyers, direct mail solicitations, customer research, product brochures, posters and point-of-sale material, and other forms of communication which are commonly used to market spirits and wines. Such a narrow interpretation is impractical and would severely limit the Commission's ability to carry out its legislative mandate.

Additionally, other promotional activities, which often prove more cost efficient and effective than strictly newspaper or broadcast advertising, would be prohibited using such a narrow definition, as well.

It is well known, within the industry, that the proper shelf management of spirits and wines is a significant and compelling factor in the marketing of these products. How products are shelved, displayed, and otherwise promoted within the Commission's retail store's environment, has a dramatic

OBSERVATION NO. 21 (Continued)

impact on sales. Which products receive the most shelf space and how they are positioned is based, in part, on the customer recognition they have received from advertising and marketing.

The Commission's shelf management program is clearly a marketing related function. Its purpose is to maximize customer purchases, by leveraging product awareness while minimizing excess inventory.

It is the view of the Commission that the shelf management program was of such significance and priority to justify utilizing funds categorized under the term "advertising" for use in this manner.

The Commission determined that it would be in the best interest of the state, and in keeping with legislative and regulatory intent, to allocate funds for the shelf management program and to consider this activity under the auspices of marketing.

Most importantly, the Commission consulted with the Attorney General's Office with respect to the utilization of the advertising funds and the contract award for the shelf management program. Additionally, the Commission discussed this issue with several members of the Executive Council. Based on these discussions, the Commission believed the contract award to be both permissible and appropriate.

This action was outlined in a letter issued to the advertising contractor, dated June 23, 1994 (and provided to the LBA), which directed them to allocate the necessary funds for this initiative.

The LBA further observes that the expenditure of $8,972, over a two-year period, used in connection with an employee sales contest, was inappropriately dispersed from the advertising budget.

The Golden Knife Awards, (named for the knife used by employees to cut product cardboard cases to create actual displays), was developed to encourage and recognize state employee excellence in creating product displays which generate consumer interest and increases in product sales.

It is a widely accepted fact, within the industry, that proper product displays have a dramatic impact on sales. Without question, product displays are a merchandising function which are part of the overall marketing function with respect to the Commission's marketing efforts.

The Commission believes that this product display award was valuable in educating employees on the importance of product displays and bolstering employee morale.

OBSERVATION NO. 21 (Continued)

Most importantly, the program stimulated Commission sales during the all-important holiday season, and contributed to creating a strong sales culture within the agency. It should be emphasized that these types of initiatives are standard, and are widely used practices within the spirit and wine industry. In fact, we intend to expand the awards dinner to recognize other critical contributions store personnel make to the State Liquor Commission's success.

The small amount of funds used to encourage state employee sales strategy excellence pales in comparison to the enormous benefits this program created.

For future clarification, we believe that the contract language should incorporate more contemporary language that would include activities related under the overall auspices of the marketing umbrella. The LBA's observation, while quick to point out the fact that the contract was perceived to be used for non-advertising purposes, fails to address the broader issue of the need for more contemporary language.

Action:

In the FY 96 and 97 budgets, the Commission has amended the classification of "Advertising" to "Advertising/Merchandising" and has supplied a definition incorporating merchandising into the appropriation. All future advertising contracts will make clear what is meant by the term as recommended.

OBSERVATION NO. 22 NO-BID CONTRACT INAPPROPRIATELY AWARDED TO MIS DIRECTOR

OBSERVATION NO. 23 CONFLICT OF INTEREST FOR MIS DIRECTOR IN ACCEPTING SHELF MANAGEMENT CONTRACT

OBSERVATION NO. 25 BREACH OF ADVERTISING CONTRACT TERMS AND CONDITIONS

AUDITEE RESPONSE:

We do not concur with the observation of the Legislative Budget Assistant Audit Division with respect to the contract awarded to the Commission's MIS Director.

The contract referred to by the LBA was for the development of a shelf management computer program critical to the proper merchandising of spirits and wines. For over one year, the Commission reviewed the need to develop a more appropriate shelf management system.

The proper management of product in the Commission's retail environment has a dramatic impact on sales. The shelf management program would provide a more consistent and defined method to the shelving of product, as well as the overall inventory mix.

For some time, industry representatives had approached the Commission with respect to providing shelf management assistance. However, the Commission concluded that implementing a shelf management program sponsored by a particular distiller would provide an unreasonable advantage in shelving and would not be sufficiently objective.

Shelf management programs available from outside, independent sources were significantly more expensive and priced in excess of $50,000. (The Commission had only allocated $30,000 for this program.) Moreover, there were serious questions regarding the reliability and deliverability of these programs and the capacity to interface with the Commission's existing computer system. Given the difficulties the Commission (as well as other state agencies) has had with computer system program integration, the Commission was appropriately concerned about purchasing a software development system that would fall short or fail in execution.

After lengthy discussions and deliberations, it was proposed that the Commission's MIS Director, given his substantial expertise of the Commission's computer system and knowledge of the agency's principal business mission, would be the best person to undertake the shelf management project. It was further determined that, given the massive scope of effort required, the project could not be developed as part of the MIS Director's regular duties, but would be undertaken as a special consulting engagement.

OBSERVATION NOS. 22, 23, 25 (Continued)

Again, it is important to point out that the Commission deliberated often and openly regarding this matter. Numerous discussions were conducted among both the entire Commission and staff members regarding this project. Certainly, the Commission would not have undertaken such a high-profile project utilizing the contract services of the MIS Director if it believed such an action was inconsistent with state regulations or law.

Most importantly, the Commission conferred with the Attorney General's Office regarding the appropriateness of using the advertising agency and funds allocated in the advertising contract for the shelf management program. These discussions are recalled by all members of the Commission serving at that time, as well as current and retired staff members.

At the suggestion of the Attorney General's Office, several members of the Executive Council were subsequently advised of the project and the suggested funding and contract method. A former member of the Council does, in fact, recall the telephone discussion with the Commission Chairman regarding the shelf management program.

The Commission memorialized the basis for its decision, as well as our understanding of the discussion with the Attorney General's Office and Executive Councilors in writing, as part of the funds allocation authorization. Certainly, the Commission would not have taken such unanimous action if there was any doubt whatsoever regarding the appropriateness of the decision.

At the time no objection was raised over the contracting of the MIS Director to undertake the shelf management program. The Commission believed that both the Attorney General's Office and members of the Executive Council concurred with our decision with regard to this matter. Again, had there been any question regarding the appropriateness of this action, the Commission would not have proceeded.

It was the Commission's intent to find a workable solution to a difficult technical and financial problem.

The Commission acted in good faith in its effort to save the State of New Hampshire well in excess of $20,000 and receive a workable and viable shelf management program. In hindsight, the Commission should have taken greater care in documenting its decision-making process.

The Commission believes that service provided for this highly technical merchandising program was best and only available from one source. The Commission does not believe it violated RSA 21-I:11 (III) with respect to this project.

OBSERVATION NOS. 22, 23, 25 (Continued)

Action:

In the future, the Commission will implement a more formalized approach to budget transfers and procurement contracts of this nature by following regular state procedures.

OBSERVATION NO. 23

CONFLICT OF INTEREST FOR MIS DIRECTOR IN ACCEPTING SHELF MANAGEMENT CONTRACT

AUDITEE RESPONSE:

See pages D-61 thru D-63 for the SLC's response.

OBSERVATION NO. 24

OWNERSHIP OF INTELLECTUAL PROPERTY IN QUESTION

AUDITEE RESPONSE:

We concur with the observation of the Legislative Budget Assistant, Audit Division, with respect to the ownership of the intellectual property in question.

The MIS Director noted each invoice as stated in the observation to prevent the distribution of Shelfman by third parties.

Specifically, the MIS Director has transferred all rights to the source code, compiled code, documentation and use for any purpose of the computer programs known as "Shelfman" to the State of New Hampshire Liquor Commission.

OBSERVATION NO. 25

BREACH OF ADVERTISING CONTRACT TERMS AND CONDITIONS

AUDITEE RESPONSE:

See pages D-61 thru D-63 for the SLC's response.

OBSERVATION NO. 26

NONCOMPLIANCE WITH STATE PURCHASING REQUIREMENTS

AUDITEE RESPONSE:

The Commission concurs with the observation of the Legislative Budget Assistant, Audit Division, with respect to non-compliance with State purchasing requirements.

The Commission was advised by the then Administrator I that the purchased goods referred to were actually replacements for existing goods already in place. We were advised that, as such, replacements did not need to follow a formal competitive bidding procedure, but rather would be obtained by requesting quotes from several vendors.

The Administrator I indicated the separate $1,000.00 or less invoice amounts were as such because she purchased items such as the window replacements as funding became available. The Administrator I, since retired, advised the Commission that quotes were received for these purchases and placed on file. We have not been able to locate these quotes.

The Commission accepted this understanding in good faith in as much as it was presented by the Administrator I in charge of procurement who had been employed in that position for many years.

Action:

In order to prevent such procurement occurrences from happening in the future, the Commission has developed policies and procedures which reinforce the utilization of competitive bidding process on all purchases which in the aggregate will exceed $2,000.00.

Further, on purchases of $500.00 to $1,000.00 signatures will be required by the Division Director and shall be reviewed and approved by the Finance division, and will require the signature of either the Director of Financial Management or the Chief Accountant.

On purchases of $1,000.00 to $2,000.00 the Finance division shall forward the requisition to the Commission for review and approval by the Chairman and Commissioners before any "order" will be processed.

OBSERVATION NO. 27 NONCOMPLIANCE WITH STATE LAWS REGARDING TEMPORARY AND PART-TIME EMPLOYEES

OBSERVATION NO. 28 ABUSE OF STATE LAWS REGARDING APPOINTMENTS TO THE CLASSIFIED STATE SERVICE BY LIQUOR COMMISSIONERS

AUDITEE RESPONSE:

We concur in part with the observations. The LBA Audit claims that RSA 98-A:6-a requires permanent part-time employment of 30 hours per week before an employee is entitled to elect to receive benefits.

We do not concur. The RSA states that, if it is anticipated an employee will be working for 30 hours or more for more than 6 months, then he or she is entitled to collect benefits. The Commissioner, Director of Stores and Store Manager recognized special talents in this individual's creative abilities and wished to avail this agency of the benefits accruing from those talents for an extended period of time beyond the 6 months as indicated in the statute and, therefore believed the individual to be entitled to benefits.

Notwithstanding the above, the Commission was not aware of any statute, personnel rule or regulation indicating the State Division of Personnel has the authority or the need to determine in lieu of the department or agency involved as to the number of hours a specific employee is needed to work, nor a requirement for prior approval for such working hours. The authority and approval requirements seems to be in place by practice rather than by written authority. At best, this silent and implicit practice was not known by the Commission staff. There have been numerous part-time employees through the years, and even during the audit period in question, who worked beyond the 30 hours stated. The audit fails to note this fact, but singles out this one instance.

Also, we were not aware of any statute, rule or regulation that requires approval by the State Division of Personnel to pay medical and dental insurance premiums. Again, if so, it appears to be implicit by practice. If there is a prior approval process, then we were not aware of it. Therefore, the confusion and action taken by the State Liquor Commission is understandable.

The Liquor Commissioners as stated did not intercede on the employee's behalf. One Commissioner states that he acted in behalf of the employee's interests at the employee's request and his request only. The indication that the employee's wife is an official of a political party organization is coincidental and not pertinent to the observation of non-compliance with state laws regarding part-time employees. She well could have been anybody, have any job, any office, private or public, or be a housewife. The point is that the agency acted on the employee's request, on what both the employee and agency believed to be what the employee was entitled to, not because of any purported or implied influences.

OBSERVATION NOS. 27 and 28 (Continued)

The Commission felt that the audit claim regarding Chapter 261:1 requiring agencies with open full-time positions did not apply. The Commission understood this to be a temporary position, not an open permanent full-time position, and believes the citation to be inappropriate. The Commissioner believed we had up to one year to make the determination whether the position would be permanently needed, and at that time would have to request the permanency to the Personnel Division and, if approved, would have posted the availability of this position and would, in fact, offer it to previously laid off employees. This belief emanated from information provided to the Commission by the Office Manager in charge of the Payroll division (and its incumbent work responsibilities), as well as from the Director of Stores. The Commission did approach Personnel with this request, and it was denied. We were then notified that the Department of Personnel needs to approve temporary employees to work more than 30 hours and also for medical benefits, and such would not be granted. When the full Commission became aware of the problem, the employee's hours were immediately reduced to below 30 hours, and his medical benefits were canceled.

Nonetheless, it would appear that the employee's spouse, upset with the treatment her husband was given, called the Governor's Office to protest. A staff member called the State Liquor Commission Chairman to find out what happened and why, was advised accordingly and was further recommended to talk with the Division of Personnel to assure that our action to stop benefits was appropriate.

In Summary:

The Commissioner directly involved unequivocally states that there was no outside political influence regarding this matter. The request came directly from the employee involved, and the actions therefore taken were done so after receiving advice accordingly from the Agency employees charged with those responsibilities. Their advice was given based on past and then present practice and their interpretation of existing statutes. The lack of clear statutes and personnel regulations addressing this issue seemed to make this advice and action appropriate. The inability of the State Liquor Commission to note and follow silent but implicit practice that may have been known by other agencies but not known by the State Liquor Commission was understandable.

Action:

The Commission will reinforce the policy in place which prohibits, for any extended period, temporary employees working beyond 30 hours per week.

OBSERVATION NO. 28

ABUSE OF STATE LAWS REGARDING APPOINTMENTS TO THE CLASSIFIED STATE SERVICE BY LIQUOR COMMISSIONERS

<u>AUDITEE RESPONSE:</u>

See pages D-68 and D-69 for the SLC's response.

OBSERVATION NO. 29

PREFERENTIAL TREATMENT OF LOCAL LIQUOR MANUFACTURER

AUDITEE RESPONSE:

We concur in part with the Legislative Budget Assistant, Audit Division, with regard to preferential treatment of a local liquor manufacturer.

We do not concur that the treatment of the local liquor manufacturer was preferential. Specifically, the local manufacturer's license includes their ability to operate their own warehouse as part of their manufacturing operation. Further, their operation and warehouse function is recognized by federal authorities as well, witnessed by the federal granting of their licensing as a bonded warehouse facility.

The local manufacturer questioned the need and the State Liquor Commission's ability to force him out of his own warehouse located within 20 miles of our state bailment facility. This would force bailment charges to his operation for a purpose he already could accommodate and which was allowed under his license. He further claimed that to force him out of his bonded warehouse to the state facility would force immediate payment of federal alcohol taxes in excess of 1/2 million dollars, an expense he could not sustain for a 2 to 3 month period and, therefore, he would have to go out of business.

The Commission, on the other hand, needed product at our warehouse in order to efficiently stage the product to conform to our distribution system to our 68 retail stores in a cost effective manner.

Accordingly, the Commission and the manufacturer reached an agreement that would require his delivery of product from his warehouse to ours three to seven days prior to our need to distribute to our stores. This would allow us the ability to stage product delivery to our stores in an efficient and cost effective manner.

The Commission in 1993 introduced a "Liquor/Wine/Beverage Warehouse License" that would allow all warehouse licensees to warehouse product but require shipment to the Commission central warehouse for subsequent distribution similar to what was being done in this case.

It is important to note that no vendor or manufacturer is directed to utilize our warehouse. They have choices, and advise the Commission as to where and in what warehouse they wish to store product. Commission approval is granted simply so we can be aware of where each product line is located.

Action:

The State Liquor Commission will adopt a written policy concerning bailment and bailment charges and apply the policy equally to all manufacturers.

OBSERVATION NO. 30

INSUFFICIENT COMPLIANCE WITH STORE OPERATIONS MANUAL

AUDITEE RESPONSE:

The Commission concurs with the observation and recommendation. The Commission and Director of Store Operations have updated several sections of the Store Operations Manual. When the Director of Stores was hired in February he was given the Operations Manual as a top priority. Store Operations Manuals have been requested and received from all the control states. We have received eight manuals to date. As each section is studied, reviewed, and updated these manuals provide a helpful comparison in establishing and updating our policies.

A new policy is in place concerning bank deposit procedures. The entire cash handling procedure was studied and completed August 31, 1994. When selecting a depository Bank, the Commission policy is to use the Bank which is located closest to our store.

The final manual will be divided into five key areas; Employee Information, Cash Control and Security, Shrinkage and Inventory Control, Building and Equipment, and Licensee Procedures. Each section requires approximately sixty days to complete. The entire manual will be complete in 1995. A priority has been assigned to each section with cash controls receiving first priority. As each section is complete, training is provided to all employees by Managers and Supervisors.

The Personnel Director and the Director of Stores are currently conducting regional meetings on sexual harassment, inventory control, and bomb procedures. Additional training seminars are scheduled to begin April 4, 1995 and will be offered to individuals that will make good trainers.

The Commission concurs with the observation concerning unauthorized persons allowed in backrooms (storage areas) of State Liquor Stores. Members of Store management risk a letter of warning for this violation.

The Commission concurs in part with the recommendations concerning the size of displays. Case displays and point of sale materials highlight consumer value. This concept enables stores to build impactful displays, feature more products during sale periods, which enables stores to satisfy customer demand, promotes impulse buying and adds fun and excitement to the shopping experience. The current trend with major discount retailers is not to restrict height. The products of NHSLC are not conducive to high stacking but often point of sale materials are used to create eye catching displays. High theft items, pints, nips, etc... are located in close proximity to our cashiers which limits exposure to theft. Stores re-merchandize and relocate attractive displays continuously to give the store a fresh look and new excitement, this promotes the customers desire to shop the entire store.

OBSERVATION NO. 30 (Continued)

The operations manual has been updated to include the following:

Floor displays must allow 40" clear aisle space to satisfy the American Disabilities Act and allow access for customers and shopping carts. Case and rack displays set-up at the end of an island type gondola must not exceed the width of the base steel shelf.

The Commission does not concur. Placing a height restriction on store displays. Store employees must continue to plan eye catching displays and stimulate impulse sales.

OBSERVATION NO. 31

POLICIES AND PROCEDURES NEEDED FOR DEPOSIT WITHHOLDINGS

AUDITEE RESPONSE:

The Commission concurs. On May 26, 1992 the Commission submitted a request to increase the change fund from $60,000 to $80,000, to the Governor and Council through Administrative Services. Administrative Services wouldn't put the item on the calendar until we reduced the request to $68,000. The Commission feels that it would be appropriate for the Governor and Council to empower the Commission to make this type of decision.

The Commission will submit another request to increase the change fund to the appropriate level to the Governor and the Executive Council.

OBSERVATION NO. 32

SECURITY OF STATE LIQUOR & WINE OUTLET STORES MAY BE INSUFFICIENT

AUDITEE RESPONSE:

The Commission concurs that security measures in stores need to be constantly reviewed. An Investigator from Enforcement and a representative from Honeywell Security Systems are visiting all stores and recommending additional improvements to store security. Alarms will be installed in all new stores and funding requested to supplement and add systems in existing stores.

Maintenance of the systems has been contracted with Honeywell. The majority of false alarms are related to equipment problems and repaired immediately by Honeywell.

The expense of additional security equipment and service contracts must be weighed against the record of past store losses (which is a very low .044%, versus the typical retail outlet loss of 1.9% of sales) and the total cost of installing and maintaining the alarms.

The NHSLC has a favorable history concerning break-ins in the 68 liquor stores. Activity for the past five years is the following:

1.	Store 11, Lebanon	7-90 and 7-91
2.	Store 7, Littleton	12-93
3.	Store 31, Manchester	4-94
4.	Store 1, Concord	5-93
5.	Store 43, Farmington	5-89, 7-89 and 10-91

Entry was gained through the front door at Store #7, Littleton in December 1993. The lock core was removed from the door. The robbers left the store through the rear door causing damage to that lock. When repaired two wooden 2x6's were installed with heavy gauge steel angle brackets. Recently pins were provided in each angle support to prevent removal of the wood. The rear door mentioned in this observation contains three steel plates and is of better quality than most stores. The store operations department has updated the list of personnel that have access to store keys and safe combinations. The list will be maintained at the central office.

In late 1993, the Chief of Enforcement was instructed to designate one investigator to work with the Director of Store Operations on security issues.

The officer who was specially trained, at Commission expense, recently took a higher paying job in the private sector doing retail store security. A replacement is being trained.

OBSERVATION NO. 32 (Continued)

Currently enforcement is actively investigating issues at four different locations. In March one employee was found guilty of theft and the NHSLC recovered $1,725.19. In April another employee was charged with Tampering with Public Records or Information, found guilty, and ordered to make restitution of $1274.00 to NHSLC. Despite the low level of losses, the Commission is quick and effective in responding whenever a problem is uncovered.

OBSERVATION NO. 33

INSUFFICIENT SECURITY FOR THE CONCORD WAREHOUSE

AUDITEE RESPONSE:

Item 1.

We concur in part that the Concord warehouse is operating without sufficient security.

Employees and outside parties ingress and egress are not adequately controlled or monitored by warehouse management.

Present contracted security services for the warehouse consist of parameter/perimeter burglary monitoring for unauthorized entry into the warehouse after the close of business hours.

We do not concur in part. The Enforcement Division acknowledges theft from within the warehouse is a concern, but there has been an assessment done and recommendations made to the Commission to better address the security issues. They are as follows:

1. Exterior lighting was addressed and corrected for better illumination during the evening hours.

2. Bushes along the building exterior walls have been removed to eliminate areas of camouflage.

3. Interior connecting doors between the warehouse and store #1 have been secured and linked to the security system.

4. The supervisor has directed that the northern exterior glass door and interior warehouse door remain closed at all times. The interior warehouse door will be equipped with a crash bar for employee emergency exit as soon as possible.

5. The Enforcement Division is presently assessing a policy for review and implementation, which would require that:

    a. The entrance near the warehouse administrative office be utilized by all employees and outside parties as the only means of entrance and exit to the warehouse;

    b. Existing warehouse administrative offices be relocated or arranged so an employee is situated directly next to the door where they may directly observe all parties entering or exiting the warehouse at all times;

OBSERVATION NO. 33 (Continued)

c. A sign-in sheet be utilized for outside parties listing their name, company name, date, time of entry and time of exiting. All non-employees shall be issued a visitor ID badge which shall be conspicuously displayed on their person; and

d. The entry door leading to the warehouse be secured at all times, preventing unauthorized personnel from entering the warehouse. This door will be monitored by a video camera.

This short term plan should be implemented in the immediate future, but will require financial support presently not available.

Item II.

We concur. The present system at the Concord warehouse operates basically on an honor system whereby employees might exit through one door, but are not monitored by warehouse and transportation management.

If an employee violates policy, by not exiting through the proper location, leaves a secured door open, etc., then the warehouse and transportation administrative management should address these situations immediately.

Considering the above assessment and recommendations made by the Enforcement Division, the SLC expects to correct existing concerns.

Item III.

We do not concur. The exterior door was installed to provide entry to the wood workshop. The exterior door is linked to the perimeter burglary system monitored by Honeywell.

An interior sliding door connecting the wood working shop to the warehouse does exist. The door is only utilized during normal business hours when it is necessary for maintenance personnel to make major repairs within the warehouse. When the sliding door is not being utilized, it is closed and secured with a keyed lock from the warehouse side, as well as being connected to the alarm system after business hours and a padlock and hasp on the woodworking side.

Item IV.

We do not concur. Warehouse security has been made a priority and we feel the foregoing actions display corrective measures taken by the SLC. The low rate of loss is testimony to our effectiveness.

Financial constraints have limited the SLC in installing and implementing other security measures to further reduce the risk of theft. Money has been requested in the Capitol Budget to cover costs of implementing security measures.

OBSERVATION NO. 34

INSUFFICIENT SUPERVISORY REVIEW CONCORD WAREHOUSE

AUDITEE RESPONSE:

The Commission concurs in part with the observation and recommendation. We disagree with the $527,104, loss due to breakage and adjustments outlined in your observation. Our records indicate that breakage and adjustments at the Concord warehouse provided a net gain in inventory of $268,038, during the past seven years. This is a result of losses due to breakage of $192,760 and inventory overage adjustments of $460,798. The inventory overage adjustments were largely due to a temporary change from 12 bottles per case to 15 bottles per case on certain product codes. The balance most likely came from either pick or clerical errors.

Because this is a closed distribution system, inventory gains in the warehouse should be offset against shortages in the stores. The total system, stores and warehouse, lost an average of $85,620 per year from adjustments during the seven year period studied, while sales averaged $193.8 million during the same period. The average inventory shrink or adjustment is only .044% of sales compared with the retail industry average of 1.9%. Sound business practices require management to make intelligent decisions relative to the cost of control processes and the associated risk or exposure that those controls might reduce or eliminate.

Concord warehouse breakage averaged $27,537 per year for the seven years studied. This represents a meager .014% of sales. This is a remarkably low number considering the warehouse is undersized, the racking inadequate and the equipment old and obsolete.

The following responses will address the six specific concerns outlined in this observation:

First, we believe supervisory review does occur as part of the receiving process. A receiving report is completed by the person unloading the truck. This report includes product code number, product description and quantity. The warehouse superintendent or his assistant check the trucking company manifest against the receiving report. Often, the manifest lacks product detail giving only cases for the entire load or no case totals at all. Ideally, all pallets could be taken off the truck and segregated until the receiving report and trucking manifest are verified. Unfortunately, space limitations force liquor receivers to put each pallet away as it is taken off the truck. This makes reconciliation of variances more difficult.

Second, the Accounting Technician is responsible for the entry of receiving slips into the computer inventory system. The Administrative Assistant audits the computerized receiving report edit against the receiving slips. We send a copy of the computer receiving report to the vendor so they can verify our receiving information against their shipping log.

OBSERVATION NO. 34 (Continued)

Third, when labels are generated for inventory that is out of stock, the product is placed on "L" status by the warehouse superintendent. This means that the book inventory says product exists but cannot physically be found on the floor. No adjustment is made to the inventory at this time. An effort is made to find the discrepancy between book and actual. Unreconciled items are adjusted at year end.

Prior to recent budget mandated warehouse staffing reductions, orders were checked by the chief shipper/receiver. The process required pickers to place orders on carts in case lots of 40 (5 long x 4 high x 2 wide) with codes facing out on both sides. After these cases were checked they were off loaded by hand onto the trailer floor. Palletizing the loads is far more efficient but makes counting and verification of cases shipped almost impossible. Pallets would have to be broken down by the checker in order to verify cases stacked in the interior of each tier. It doesn't appear to be a good use of the warehouses limited resources when you consider the rate of mispicks is less than .5% and most shipments are within a closed distribution system.

Fourth, as stated earlier, reductions in human resources has made timely reconciliations of missing items difficult. The first priority of the warehouse is to get product out to the stores and licensees. The warehouse is operating in an under staffed environment and some task will not be completed in a timely fashion. In the past, the Commission has requested additional staffing to strengthen the inventory process in both stores and warehouses. Budget restrictions have made funding for this type of activity impossible.

Fifth, the warehouse does do cycle counts when time permits. On average a cycle count of 30 items is performed every two weeks. Budget restrictions have limited the labor hours available to take inventory.

Finally, warehouse management is well aware of the problems associated with palletized shipping of glass and plastic product. Currently, the warehouse picking area is laid out so the high volume items require the least distance of travel for the picker. The computer generated picking labels come out in order of where the product is found in the warehouse starting closest to the loading dock. Isles are one way because they are too narrow to allow loaded pallet jacks to pass each other. The picking flow is continuous so a picker never has to retrace his steps. The warehouse could be laid out so that all glass products are first in the picking route but that would create inefficiencies when picking plastic. Many of our highest volume products are packaged in plastic. We are planning to experiment with the picking area after the first of the year by locating high volume glass, then high volume plastic, followed by low volume glass and then low volume plastic.

OBSERVATION NO. 34 (Continued)

Further more, warehouse employees do try to interlock cases as opposed to straight stacking, but cases are not of a standard size which makes interlocking of each tier virtually impossible. The contract trucking company is responsible for providing tape or rope for securing cases on each pallet. The tape is a black packing tape designed for this use and works well in most cases. Shrink wrap is not covered under the trucking contract and would have to be purchased by the state. Shrink wrap is expensive, time consuming to apply, requires investment in application equipment and products a lot of waste that stores would have to dispose of. When you consider that the trucking company is responsible for any breakage that occurs in transit, it doesn't seem cost effective to the state to spend a great deal of money to resolve this issue.

LBA REBUTTAL:

We do not accept the agency's numbers as reported. The agency-reported net gain is derived from gross losses and overages which include two warehouses not directly operated by the SLC. Ironically, when the grosses for only the Concord warehouse are used as we have, there is a net gain of $466,664 ($198,626 more than reported by the agency response). We report $527,104 in gross losses for the period FY 1988-1994, from data provided by the MIS division. This is the sum of $334,459 in inventory shortages plus $192,645 in breakage. Gross losses were offset against gross overages in the amount of $801,103 for the same time period. Again, these numbers are for the Concord warehouse operation only.

The switch from 12 to 15 bottles for some product codes had no effect on the Concord warehouse. According to the warehouse superintendent, the switch occurred with products warehoused at the privately operated Nashua facility.

The agency's average shrink rate is commendable. However, we do not accept the size of reported losses as indicative that there are no problems worth improving within warehouse inventory management procedures. An exceptional average shrink rate can hide inefficiency and other problems. Whether it is cost effective to fix these problems is obviously a valuable question to ask, but so is the question of what it's costing the agency to operate with them. Are the person-hours spent searching the warehouse for lost shipments and making manual adjustments to the automated warehouse inventory management systems acceptable costs? Would the cost of preventing problems be excessive? We don't think so.

The warehouse supervisor reported he reviews receiving documents only to ensure the correct account is used. We recommend the superintendent also regularly check quantities and brands reported as being received and compare this with trucking manifests.

OBSERVATION NO. 34 (Continued)

The administrative assistant reported she did not review the accounting technician's data entry due to time constraints. In addition, the superintendent reported no one was assigned responsibility for reviewing the accounting technician's work.

MIS management reported on several occasions that cycle counts were not done in the warehouse. MIS also resisted the idea that more inventory counts than the annual inventory be performed.

OBSERVATION NO. 35

FINANCIAL MANAGEMENT POLICIES AND PROCEDURES INSUFFICIENTLY DOCUMENTED

AUDITEE RESPONSE:

The Commission concurs in part with the observation and recommendation relative to written policies and procedures. The Commission and the Director of Finance recognize the value of written policies and procedures and have prioritized the development of a comprehensive manual accordingly. Turnover (in the past 3 years the department has had changes in the following positions: Director, Chief Accountant, General Ledger Supervisor, Payroll Officer, Accounts Receivable Supervisor - twice, and other non-supervisory positions), limited human resources and other priority projects have hampered progress on this issue.

The Financial Management Division does have procedures for each function area, although many are not in writing. There are written procedures for accounts receivable, Cash Receipts, Deferred Revenue and some general ledger functions. When we hired a new general ledger supervisor in December 1993, we made learning the operating procedures of each function area her first priority. During that time, she diligently recorded procedures and made suggestions as to where improvements need to be made. Unfortunately the general ledger supervisor resigned in November to take a more appropriately compensated job. We are now training a new general ledger supervisor. We plan to continue developing written policies for each function area and then combine these into a comprehensive operating manual.

The Commission concurs with the observation and recommendation relative to the petty cash and training log. The requested changes have already been made to the filing and documentation procedures for petty cash disbursements.

The task of maintaining a training log has been assigned to the administrative secretary in the Financial Management Division. Training records for the past two years have been compiled for each employee. Completion of this project is targeted for 10/28/94.

Proper documentation and record storage and retention of credit applications, letters of credit and overdue notices began in the fall of 1993. The process has been fully implemented.

LBA REBUTTAL:

In a separate communication the agency has indicated that a comprehensive operation manual will not be available until May 1996. Without written procedures financial management has no way of knowing whether accounting functions are being performed in a manner that both reduces the risk of waste, fraud or abuse and assures the utmost efficiency within the operation.

OBSERVATION NO. 36

INSUFFICIENT SUPERVISORY REVIEW

AUDITEE RESPONSE:

The Commission disagrees in part with the observation and agrees with the recommendation. Based on our 10/14/94 conversation, the Commission understands the specific issues to be as follows:

Accounts Payable -	No data entry checking of edit to invoices on paid bills.
Payroll -	No review of keyed labor hours to source document.
General Ledger -	No review of data entry of cash receipts journal and no supervisory review over miscellaneous payments.
Accounts Receivable -	No review of credit card transactions or bank statements and no review of credit application documentation.

The first section, Accounts Payable, has sufficient supervisory review in our opinion. Approved invoices are keyed into the system. An edit is run and then checked against the invoice by the person who did the input. At the same time the accounts payable supervisor reviews the voucher & expense report for proper set-up of invoices and correct general ledger distribution. Upon acceptance the payment vouchers are run and then checked against the invoice by the unit supervisor or assistant supervisor. After the payments have been input into the integrated financial system system, (via tape) the accounts payable supervisor or assistant supervisor reviews the actual approved payment voucher report against the integrated financial system screen. Copies of all invoices and payment vouchers are sent to the Bureau of Accounts for final auditing. It is our understanding from the Bureau of Accounts that the Liquor Commission has a very low percentage of errors compared with other agencies.

We also believe that the payroll department does an excellent job of supervisory review. In the main office, each division has a person designated to input daily payroll hours and to forward leave slips to the payroll department. Payroll generates an employee payroll edit by division, by unit for each payroll week. The edit is sent to the unit supervisor with copies of leave slips attached. Each employee signs off on their hours and the supervisor reviews the leave slips and signs off on the units payroll for the week. Each unit payroll sheet is forwarded to the department head upon completion for final approval.

Store employees fill out and initial a time log daily and the store manager inputs this information into the in-store computer. This information is up-loaded into the main-frame every night and a copy of the time log with copies of leave slips attached is mailed to payroll each week. Payroll

OBSERVATION NO. 36 (Continued)

audits the time log against the payroll edit each week. Every week each division director and the Commission receives a report of discrepancies. (See Attached)

The general ledger unit supervises the Account Clerk III who is responsible for entry into the cash receipts journal. Supervisory review for this function is accomplished with documentation provided with the A-17. Attached is a copy of the deposit ticket, bank deposit slip, detail tape of checks including bank #, check # and amount and the cash receipts journal posting edit summary which are reviewed and signed by both the general ledger supervisor and the Chief Accountant. An accounts receivable edit and the entered invoices are forwarded to the accounts receivable supervisor for auditing. Errors are returned to the cash receipts journal clerk for correction. This process continues until a clean edit is obtained and the accounts receivable interface is done. The general ledger supervisor audits the Division of Accounts monthly report from the integrated financial system against the daily A-17's.

We recognize a weakness in the accounts receivable unit due to the supervisor position being vacant from August '93 to January '94. During this time we became aware of several supervisory shortfalls in this area. They would have been caught earlier if the general ledger supervisor's position wasn't vacant at the same time. The Finance Director became aware of the problem with credit card documentation review in September '94, and began reviewing all credit applications for compliance with administrative rules. This procedure was turned over to the new general ledger supervisor in February '94. The accounts receivable supervisor's position has been vacant since July '94, but has been filled effective October 24, 1994. The new accounts receivable supervisor will be responsible for conducting and documenting appropriate reviews. The general ledger supervisor position will be vacant again as of October 31, 1994. Because of personnel rules the search for a replacement will take longer than it would in the private sector.

Each year the commission is a component of a statewide financial audit performed by Ernst & Young. The FY '94 review of SLC financial data didn't produce any material procedural deficiencies that would put the commission at risk for employee fraud other than those noted above relative to credit card and bank statement reconciliations performed by the accounts receivable unit. E & Y was able to complete this years review of the SLC component of the audit in half the time of prior years due to significant improvements in our financial records.

It should be noted that the accounts receivable, accounts payable and payroll supervisors report to the general ledger supervisor not directly to the Chief Accountant. It may have appeared that these supervisors reported to the Chief Accountant because the general ledger supervisor was in training until the end of January and the Chief Accountant had to assume some of the duties of that position.

OBSERVATION NO. 36 (Continued)

If the LBA has any specific recommendations the Commission will perform a cost/benefit analysis and implement those recommendations that make financial sense provided resources are available for the implementation.

The lack of staff, not written procedures, is the reason the credit card reconciliations are behind. The person who is responsible for the reconciliations has been doing them since the program's inception 13 years ago. She cross-trained an Account Clerk III in the procedure but this person left shortly after she completed training. The accounts receivable supervisor was out on maternity leave for several months due to complications and the Senior Accounting Tech. in charge of reconciliations had to fill in for the supervisor. The general ledger supervisor position is the other back up for that function but the position was vacant for several months in fiscal '94.

The Financial Management Division has had a tremendous amount of turn over during the past 12 months. The Administrator I (Now reclassified to Chief Accountant), retired in May of 1993 after being out on sick leave for much of the previous two months. After several months of negotiating with the Division of Personnel over the proper classification the position was posted and filled internally on Sept. 30, 1993. This left a vacancy in the G/L supervisory position that wasn't filled until December 20, 1993, due to the long and cumbersome personnel process that must be followed. Effectively, the division was short this key management person for 10 months.

During this period the accounts receivable supervisor was out on an extended maternity leave, an accounts receivable Account Clerk III position was vacant due to promotion for several months, the other accounts receivable Account clerk position was also vacant due to promotion for a few months. One of the replacements worked for about 6 months before taking an appropriately compensated position outside the organization. The constant turn-over due to uncompetitive wages makes it very difficult to recruit and hold quality employees. The accounts receivable department's turn-over during the past two years has caused them to operate at approximately 50% of full staffing during that time.

Currently, a recommendation has been made to the commission to make an appointment to fill the accounts receivable supervisor position. The new supervisor will then recruit and hire a new Account Clerk III. This will put the department at full strength for the first time in several years. The general ledger and Credit Cards have been reconciled through June 30, 1994 and will be current by November 1994.

The Commission has requested overtime monies in the FY '96 & '97 budget request for this Division. This will make it possible to compensate employees that have reached the maximum allowable amount of compensatory time so that they will be available to complete critical task when there is a shortage of personnel.

OBSERVATION NO. 36 (Continued)

The Commission will be acquiring a new accounting software system that will allow more flexibility in posting and reconciliation of general ledger accounts. This project is scheduled for completion in April of 1995.

Once this high priority project is done we were planning on reviewing written policies and updating them to be consistent with the new accounting system.

The Commission believes that the Director of the Financial Management Division best contributes to the organization by setting policy, then selecting the staff to carry out the day to day implementation. The Director makes excellent use of the limited resources available to him in carrying out his mission for the state's largest business considering the bureaucratic environment in which he must operate.

OBSERVATION NO. 37

INAPPROPRIATE USE OF PETTY CASH AND CHANGE FUND

AUDITEE RESPONSE:

The Commission concurs with the observation and recommendation. Even though all reimbursements, except for the two in-state lunches were legitimate, we agree that they should have been paid according to Department of Administrative Services procedures. This problem was rectified in October 1993. Written policies and procedures will be issued on this process and incorporated into the operating policy manual that is currently under development.

OBSERVATION NO. 38

INSUFFICIENT SECURITY FOR CASH AND CHECKS

AUDITEE RESPONSE:

We do not concur in part. Enforcement and licensing programs were the first of the data processing systems implemented by the Commission. They have been added on to and "improved or amended" as needed. **The policies and procedures have been construed to be adequate in that the work gets done, money is not lost and personnel are thoroughly familiar, with the exception of those in training, of how the procedures are done.**

We do not concur with the sentence from the LBA report "Further, if the general ledger account clerk does not notify licensing and enforcement personnel that outstanding fines were paid by licensees, vendor licenses may be wrongfully suspended." No one has ever been "wrongfully suspended" because a check was not recorded properly.

After the LBA 1989 financial audit the SLC obtained permission to add the treasurer's account number to the endorsement stamp. All personnel who may have contact with checks have a restrictive stamp available to them and are required to stamp checks immediately upon receipt as outlined in a re-issued memo issued by the general ledger supervisor on 4/4/94 as a reminder of established policy.

In some areas increased costs and confusion are incurred when the Commission immediately complies with the LBA request to date stamp each application and apply the restrictive endorsement on the check upon receipt.

When an application is materially defective/incomplete, by rule it must be returned to the applicant including the check. This causes confusion to some applicants as they believe the check has been processed on the date the application was date stamped. Persons reviewing the application may believe it was processed when originally stamped or confusion may result as to when an application was processed when two dates appear. **The Commission will, however, comply with LBA's request, incurring the slight additional cost in processing.**

The following procedures are being used for processing those items:

A. The procedure currently being utilized for processing payment of fines is:

1. Record Control Clerk receives the check in the mail or over the counter;
2. Record Control Clerk opens the envelope or takes the check from the customer and stamps the back of check with the liquor commission endorsement;
3. The Record Control Clerk then:
   a. Pulls the pending fine file from their bottom drawer of the desk;
   b. Locates the violation and fine letter;

OBSERVATION NO. 38 (Continued)

c. Writes on the front of the check the letter "A" (administrative fine) a dash -, and the license number;

d. Writes on the fine letter the date check was received, check number, bank number and amount of check and their initials; and

4. The fine letter with violation is then filed in the licensees folder while the check is put in the envelope in the supervisors office to be brought upstairs with all the checks at 3:00 PM.

5. Cash payments are counted and placed in an envelope which has the "A" and license number, the name of the business and a statement that the contents is an administrative fine and the initials of the person taking the cash payment.

The fine letter has the amount received, the fact that it was cash, the date and the initials of the person receiving payment. A receipt is issued to the customer making a cash payment.

Because of the LBA recommendations, this process will be changing somewhat as MIS and Enforcement are currently working on a program for Enforcement to control and input the check information into the computer before bringing the checks upstairs. All of the above will still happen with an additional step of inputting check into computer.

B. The procedure currently being done in regards to non-payment of fines is:

1. Records Control Clerk daily checks the fine file to see if any files are due/overdue;

2. Records Control Clerk then calls licensee on the 10th day to remind them about the fine being due that day and informs them to have it in by 4:00 PM in order that their license not be suspended;

3. If they inform the clerk the check was mailed a few days ago, the record control clerk then calls the general ledger unit to find out if they received a check and posted it to the licensee's wine credit account instead of sending check downstairs to Enforcement; (This occurs when a check will come in with no notation as to what it is for and the licensee has a credit account.) If the check was improperly posted, general ledger unit will correct problem and inform us as to when the check was received along with the check information needed for Enforcement to complete their usual fine handling procedures.

4. If the general ledger unit has not received any check for that amount, the records control clerk will call licensee back, inform them it has not been received and that it must be here by 4:00 pm.

5. If the fine is not received by the close of business, the records control clerk then types suspension form to be initialed by the chief of enforcement and hand carried by investigator for service on the delinquent licensee.

OBSERVATION NO. 38 (Continued)

C. The Enforcement procedure for processing license fee checks is as follows:

1. Administrative Secretary will receive applications and check in mail;
2. The applications are:
    a. Taken out of envelope and checked;
    b. The check is then stamped with the liquor commission endorsement;
    c. The license number is then written on the front of the check;
    d. The bank number, check number and amount of check is written on the back of the application;
    e. The check is then paper clipped to the application.
3. After all applications are opened, if the application is not complete, that fact is documented, a check list stating what is needed attached and the application and check is returned to licensee to complete. If the applications are complete they are matched up with the investigation.
4. The license history card is then pulled and paper clipped to the application, check and investigation.
5. Using a typewriter, the processor updates the license history card, and staples the field investigator's investigation to the back of the application;
6. The check is put in an envelope (which is kept in supervisor's office) with other checks to go upstairs at 3:00 PM.
7. At the computer, any changes that need to be put into the computer is done, the check information is then in-putted into the computer. A license is generated (printed) at the end of the day.
8. If an application comes in over the counter, the application is viewed to be sure everything is correct and the check is then stamped with the liquor commission endorsement stamp before being given to Administrative Secretary to process. A one day license is given to the Word Processor Operator I to process.

We do not concur that the Chief of Enforcement and Licensing has not made the development and implementation of written policies and procedures pertaining to processing fees and fines a priority. A first draft training manual and work explanation/instruction explanation has been created for office and audit personnel.

We concur in part with the recommendation to obtain a receipt for cash to be placed in the safe (if only for our own protection). It should be pointed out that Enforcement has been following a procedure to the letter which was implemented by Accountant IV as to safe procedures.

OBSERVATION NO. 38 (Continued)

LBA REBUTTAL:

The observation regarding failure to observe the check endorsing procedure was based upon information reported to us in interviews with financial management and enforcement personnel who themselves receive checks.

OBSERVATION NO. 39

DISPOSITION OF PRINTER PURCHASED THROUGH SHELF MANAGEMENT CONTRACT IS QUESTIONABLE

AUDITEE RESPONSE:

The Commission concurs with the observation and recommendation. The shelf management contract was part of the advertising contract the Commission entered into with an outside advertising agency. The advertising agency entered into a subcontract with the MIS director to develop the shelf management system. The MIS director billed and received payment from the advertising contractor for the purchase of an X-Y plotter. While it was difficult for the Financial Management Division to readily determine, the original intention was for the Commission to own the X-Y plotter. We have instructed the Financial Management Division to book the appropriate entries and add the X-Y plotter to our fixed asset inventory and this has been done.

OBSERVATION NO. 40

INSUFFICIENT MANAGEMENT INFORMATION SYSTEMS POLICIES AND OVERSIGHT

AUDITEE RESPONSE:

We concur, but in particular we need to make clear that most computer policies and procedures are documented extensively in the computer for the convenience of computer users. The need for inefficient paper documentation is, therefore, minimal.

Production is very well documented and controlled in the computer environment. There are several volumes of detailed procedures for every computer program/system running in production mode. These procedures encompass both expected job sequences and error situations.

Program development is controlled on-line: it is assigned on-line; it is reviewed on-line; change requests are captured and monitored on-line; an audit of changes takes place on-line; testing takes place on-line (in a separate computer partition). Each Commissioner and each Director has a (weighty) documentation summary of the major reporting systems. We could produce a written guide, but it would be an inappropriate and unnecessary use of our resources.

With a development staff of seven, MIS supports four major operating systems, two major database systems, external and internal networks, several major applications systems, several specialized applications systems, and a whole host of other program products and external systems. For this reason, and with the resources available, the testing of programs cannot simply be routinely documented; however, all test items must be logged, scheduled and approved by the Director before they are placed in production. As far as store systems are concerned, we agree that the Siemens-Nixdorf applications programs are not as well tested (by them) as we would like, but we do test major releases extensively over a period of days before we release them into production.

All personnel receive in-service training on an on-going basis as needed, including training by in-house personnel and by seminars run by an outside consultant.

We concur with the need for an information technology plan findings and have taken steps to comply with the recommendation to work with OITM to develop an MIS plan as part of our 3 year business plan completed in August 1994.

However, we need to point out that the issues were already being addressed.

First and foremost, our Director of MIS has the most seniority of anyone in management at the Commission. His intimate knowledge of our operations (well supplemented by that of his direct reports), combined with his keeping in touch with developments in the industry, has kept our hardware and software in good enough condition to make New Hampshire the most successful

OBSERVATION NO. 40 (Continued)

control state in the country. Furthermore, there is a meeting every week between the Commission, the Directors and some of the key personnel, as needed. In this environment, we all discuss on-going needs, or needs which change due to a volatile marketplace. Software is adapted in a timely manner as resources and management focus permit. The MIS Department also keeps in touch with information and expertise available through New Hampshire, in the Boston area and throughout the country as needed. We have a record of being out in front of the curve on appropriate technology transfer. This is a necessity of the competitive business environment in which we operate, not due to demands for documentation from other government departments. The State Liquor Commission is the only retail and wholesale business in State government, and we have managed to adequately address our unique MIS needs with a limited budget and number of personnel.

One of the impediments to producing a Business Plan as a platform for an MIS plan has been the extraordinary delays in receiving a format that OITM has found acceptable in other State departments. After months of delay, we now have a somewhat acceptable example at our disposal. Nonetheless, we are producing a pro forma business plan and expect to complete a technology plan by November 1994.

LBA REBUTTAL:

The policy and procedures deficiencies we cited were pointed out to us by MIS staff. Written documentation would be helpful as a crosswalk for new users and MIS personnel for information and access purposes to the on-line documentation.

The agency response fails to address the major contentions in our observation: 1) store-based computer systems are minimally tested and no standard testing criteria exist, and 2) consistent standards regarding user and systems documentation are needed.

OBSERVATION NO. 41

INSUFFICIENT SUPERVISION OF INVENTORY TRACKING PROCEDURES

AUDITEE RESPONSE:

The Commission concurs in part and does not concur in part.

The Commission concurs that having the Supervisors/Managers review discrepancies on incoming shipments of product must be included in every store visit to minimize possibilities of human error. This reconciliation would not necessarily detect inefficient practices, fraud or abuse but the Supervisor should counsel employees on proper procedures or recommend to the Director of Stores that appropriate action be taken.

Store employees cannot make adjustments to inventory quantities. Only authorized MIS personnel may make adjustments to store inventory counts. The MIS employees do not have access to the actual products.

Store employees report variances from shipping invoices by keying into their in store processor any overages and/or shortages detected. The variance is verified by recounting the items (both shortages and overages) on two separate occasions. This enables the MIS department to match discrepancies that may have occurred in other locations and review the entire activity of the trailer load. The Director of MIS continually reviews this important aspect of the operation and advises the Director of Store Operations when a security violation may have been detected. The store and warehouse inventories are adjusted by MIS personnel depending on the results of multiple recounts, and review of the reporting.

The Liquor Commission does not concur that 3.4 million in product was potentially lost from FY 1988 through FY 1994. The warehouse and stores are part of a closed distribution system and discrepancies should be viewed for the total system. Overages should be netted against shortages to account for clerical errors and mispicks.

Year	Store (Loss)/Gain	Total Loss/Gain	Store Sales	Total Gross Sales	Store (Loss)/Gain	(Loss)/Gain
1988	(131,127)	$ -147,504	$148,638,360	$ 172,159,259	(.0882)%	-0.085%
1989	(146,229)	-148,450	154,187,682	178,894,659	(.0948)%	-0.082%
1990	(158,435)	-173,124	161,396,116	187,635,976	(.0982)%	-0.093%
1991	(135,131)	- 31,914	169,159,296	194,459,158	(.0799)%	-0.016%
1992	(125,044)	+263,064	175,998,787	204,619,296	(.0711)%	+0.128%
1993	(165,865)	-182,152	175,798,818	208,174,845	(.0944)%	-0.087%
1994	(167,453)	-179,256	175,130,688	209,749,629	(.0956)%	-0.085%
TOTAL	(1,029,284)	$ -599,336	$1,160,319,747	$1,355,692,822	(.0887)%	-0.044%

The table reflects total loss of $599,366 for the seven year period on $1,355,692,822 gross sales and store losses of $1,029,284 on $1,160,319,742. Either the combined loss ratio of .044% or the store loss ratio of .0887% is fantastic compared to private industry. Major retailers such as Wal-Mart, Sears, T.J. Max and K-Mart now consider a full point of shrinkage normal performance, while the retail liquor inventory averages 1.9%. The NHSLC is justly proud of the inventory control system in place but continues to monitor store and warehouse operations to insure losses are minimized.

OBSERVATION NO. 41 (Continued)

LBA REBUTTAL:

We do not accept the agency's numbers as reported in its response. The agency-reported net loss was obtained from data for both the warehouse and the stores operations. Using the same data for the stores, but eliminating the warehouse operations data, we arrived at a net loss of $1,052,616 ($453,279 higher than the agency's combined total). Data from MIS division-produced quarterly swing reports, which are interim management tools, indicate the agency had to reconcile potential store losses of approximately $3.4 million against potential overages of $2.1 million (a $5.5 million swing) before arriving at a loss of $1.3 million.

MIS personnel who are responsible for inventory tracking reported the MIS director does not conduct supervisory review. The senior MIS person responsible for inventory tracking reported not supervising her assistant. This was verified by the assistant. Cycle counts may be repeated as many as six or seven times according to the same personnel.

Had supervisory review been adequate the many inventory overage adjustments cited in the agency's response might have been greatly reduced. Improvements in supervisory review of inventory tracking could help improve further even the agency's reported loss ratio.

OBSERVATION NO. 42

INADEQUATE PROCEDURES FOR PROCESSING LICENSE FEES AND FINES

AUDITEE RESPONSE:

The SLC concurs with the observation and since the original observation, two things have happened in this regard:

A. The Liquor Commission respond to LBA allegations and sent a detailed outline of the procedures which are followed for processing payment of fines as well as an explanation of how license fees are handled and that fact that a system was in place for handling of these receipts. In fact the outline came from a portion of a training manual and specific task outline, which **the Administrative Assistant Chief has been in the process of developing since his appointment.**

Employees routinely place restrictive endorsements on all checks received. Each employee who receives checks has and uses a restrictive stamp. Cash procedures have been standardized as well as procedures for securing cash which is not deposited that day.

The Administrative Assistant Chief, as the unit supervisor, has as a part of the employee evaluation and professional growth process, placed a performance expectation on the Examiner II and the Administrative Secretary Supervisor to document the training process of all new employees for each position supervised so that a training and procedural manual can be developed for each job. A part of this process is an actual description of how the work is done to provide a reference manual. Although not completed, it has been drafted and submitted to the chief for review.

B. The Administrative Assistant Chief has documented the process of training, the procedures to be followed, the evaluation process, the actual work performed and has completed a draft manual for the audit section - Audit Section Training and Evaluation Program (A.S.T.E.P.) and for the clerical section - Office Section Training and Evaluation Program (O.S.T.E.P.). The cover training and cross training for each position under his supervision. The Commission would like to point out that this is the position the LBA recommends abolishing, as not needed.

The manuals were put together in conjunction with the Examiner II, Examiner I, Accounting Technician, and the Administrative Secretary Supervision working as a team and done in addition to their regular duties assigned. Although not yet complete, they are ahead of the target date set during the LBA audit.

OBSERVATION NO. 43

ENFORCEMENT AND REGULATION DIVISION LICENSEE RECORDS ARE NEITHER SECURE NOR COMPLETE

AUDITEE RESPONSE:

I. We concur in part that the Enforcement and Licensing Division Records are not complete.

1. The Enforcement and Licensing Division has been aware of the problem that some records are incomplete. The licensing documentation rules changed, effective January 1, 1992 from just requiring complete documentation on all new businesses to additionally requiring documentation on all licensees who renew licenses in keeping with the statutory change in RSA 178:24, which requires both notification and updates of any change in the application or documentation on file with the Liquor Commission.

Since January 1, 1992, on every occasion that a licensee file was noted to be deficient, investigators were required to secure the additional documentation prior to the license being renewed. In addition, when files were reviewed for consolidation or deletion of certain items, all files which were observed to be deficient, by the clerk or investigator assigned the task were referred to the Assistant Chief, who, if the file was deficient, had the servicing investigator secure the additional documentation prior to the license being renewed.

In late 1993 and the first half of 1994, Inv. S. was assigned to headquarters - at least two days a week - to review the liquor vendor, table wine vendor, liquor and wine representative, liquor and wine sales person, beverage carrier, wine carrier, beverage vendor and beverage vendor importer files, request additional documentation, if needed, and update the files. With exception of eight, the documentation has been completed. Additionally, Inv. S. had started reviewing and updating the social, veteran, college and golf club files, sending notices to the investigators to secure any needed documentation. This project has been transferred to Sr. Inv. P. It is the Enforcement Division's intent to review each file until all needed documentation has been secured.

The Chief of Enforcement and Licensing had started this project long before the LBA audit when Assistant Chief F. came into the office. They have upgraded the project's priority depending on the availability of staff to work on it. Because all new businesses have been supplying complete documentation and investigators are responsible for updating files continuously in their own areas, we do not anticipate as many omissions in the hotel, restaurant, or off-sale folders as in the ones we have completed to date.

OBSERVATION NO. 43 (Continued)

Although there are some problems with our records keeping, we believe that our recognition of the problem and implementation of a program to correct the situation, under the current Chief of Enforcement and Licensing, using the limited resources available to us, should be considered in alleging any non-compliance with RSA 5:33, III.

2. To our knowledge, only one licensing file was missing when LBA requested it and that one file had been out of business for some time.

3. The current Chief of Enforcement and Licensing, upon being named chief and after advising the commissioners, changed the system which he inherited with regard maintaining out of business files to protect the state's legal rights.

The Enforcement and Licensing Division is currently storing all out of business files in a locked area in the commission warehouse. They will be kept on site for a period of seven years (concurrent with the limitations on civil process). No determination has been made to date to destroy or ship the documents to archives after seven years.

II. We concur in part that the Enforcement and Licensing Division Records are not secure, however the Enforcement Division has taken steps to solve the problem.

A security wall, electronic and manual locks and a security door have been installed at the entrance to the Enforcement and Licensing section. The gate is accessed by key cards which record the person's name and time of entrance. Staff and the Human Resources Coordinator only have access one half hour prior to work and one half hour after work. The Chief of Enforcement and the Administrative Assistant Chief have 24 hour access. Not even the Commissioners have access to the records once the last person from enforcement leaves the area and locks the door.

Other security measures were discussed with the commissioners some time ago by the Chief of Enforcement and measures have been taken to control access by individuals going to and from the Human Rights Administrator's office. A policy states no employee shall leave exposed materials on an unattended desk. Material waiting to be filed was turned bottom side up to make it less available for inspection.

A sign-in and badge system for visitors entering the building has been instituted whereby visitors are not allowed to simply wander about the building, but are signed in by the receptionist and are escorted by the person they wish to see to and from the persons' work area - including family members.

OBSERVATION NO. 43 (Continued)

Enforcement and Licensing also recommended that certain alterations be made to the front counter area to better control access to the building as well as recommending that the Human Resources Administrator be moved out of the Enforcement and Licensing areas to a more appropriate location, which would not compromise file security. Currently this recommendation is cost prohibitive to implement.

Due to fiscal restraint money has not been available to replace the Enforcement and Licensing records "Lectriever" file cabinet, but money has been requested by Enforcement and Licensing for the next budget year to replace the unit with a similar larger securable one.

Enforcement and Licensing is currently studying the development of a system to better control files, both as to what kind of a system might be implemented and how it will be accomplished.

OBSERVATION NO. 44

ADDITIONAL ADMINISTRATIVE RULES SHOULD BE PROMULGATED

AUDITEE RESPONSE:

The Commission does not concur with the observation or recommendation. We don't believe that Administrative Rules are required by statute for the bailment operation. The Commission does have written policies and procedures for vendors using the Concord bailment warehouse.

The Commission is unaware of any bailment related complaints from vendors since the inception of bailment at the Concord warehouse on December 1, 1990. By issuing policies instead of adopting administrative rules, the Commission retains the ability to operate efficiently in a dynamic business environment.

Furthermore, the Liquor Commission has adopted rules with regard to suspension of licenses in Chapter 600 and specifically in Part 603 - **ADMINISTRATIVE PENALTIES**.

The Liquor Commission has been recognized by the administrative rules committee during the rulemaking process as being a quasi-judicial body which makes decisions based on the type of violation and specifically defined criteria for aggravating and mitigating circumstances which are considered as part of the adjudicative process (**Liq Part 207 PROCEDURES AND CONSIDERATIONS AFTER ADJUDICATIVE HEARINGS**).

The Joint Committee on Administrative Rules has recognized that one cannot quantify how each Commissioner considers these factors in their mind when they voted to approve the current rules after the Commissions response to their preliminary objection.

The outcome of any vote on a given issue will vary with the person and will subsequently affect the penalty imposed. These individual thought processes and considerations cannot be quantified to cover all situations and still allow judicial latitude. The legislature has recognized latitude is necessary for justice. They do not set specific and determinate penalties for all violations of law, but broadly assign laws into certain categories, labeling them as violations, misdemeanors (A & B) and felonies. There is even further latitude within these groups for the imposition of actual penalties based upon the totality of the circumstances.

The Commission has adopted rules of practice as required by RSA 541-A, has had those rules voted on by the Joint Legislative Committee on Administrative Rules, answered their preliminary objections and did not adopt the rules until the committee voted their approval of the response. During the rulemaking process, the committee recognized the need for latitude in the Commission's decision making and penalty imposition process.

OBSERVATION NO. 44 (Continued)

The critical steps in this process are briefly outlined as follows:

1. Liq 206.03 **Adjudicative Pre-hearing Requirements of Licensees** requires the licensee to provide an administrative plea within 5 working days after the investigator issues a "filed administrative notice", if they want a hearing.

2. The Chief of Enforcement is required to try to negotiate a good faith settlement of the issues (Liq 206.05(a). Once a settlement is agreed to the presiding officer causes a statement agreement to be drawn to specify the terms and conditions of the settlement.

3. Once the Commission votes to accept the negotiated settlement or after an adjudicative hearing, within the time constraints set by rule, the Commission issues an order as prescribed by Liq 206.11(f). A part of that order is the imposition of the penalty (fine, suspension or a combination of both). In addition and still a part of that order is, who a fine shall be paid to, when the fine shall be paid and the consequences of non-payment of that fine. Most fines are issued in lieu of suspension as allowed by RSA 179:57.

Due process, as required by RSA 541-A is not circumvented, the procedures are outlined in rule as required.

We concur in part that the rules could be clearer with regard to the commission order of payment of fines and subsequent suspension of the license if the fine is not paid, but do not concur that the 10 day period has to be specified in rule, if it is set as a condition of an agency order or settlement agreement. The Commission agrees that the concerns of LBA could be addressed in a future rulemaking session.

We do not concur with the third portion of the observation which refers to wine tastings. The first of these occasions was a tasting held at a licensee in Portsmouth on February 3, 1994. The tasting featured the owner-operator of a winery in France. The world-renowned wine-maker was traveling with a presentation of his old vintages to be tasted to demonstrate his house-style. We were fortunate that New Hampshire was included as a stop on his national tour which is normally limited to markets such as Boston.

In order to accommodate the visit of the vintner to our state and the Pease Trade Port, the Commission concluded that it would be fair and reasonable to collect our gross profit on each of the unlisted wines tasted. The Wine Marketing Specialist was asked to review the submitted price estimates and after reviewing all sources at his disposal, concurred. In comparison with the fee charged by the Commission, $6.15 per bottle, the actual calculations based on the two wines, out of the six that were later submitted for listing in the state, the fees should have been $2.55 and $1.78 respectively. The observations by the LBA auditors were therefore inaccurate when implying that the vendors somehow were not charged the appropriate price. In fact, they were charged three times what they ordinarily would have been charged.

OBSERVATION NO. 44 (Continued)

The second instance was a dinner and tasting held at a licensee in Amherst on March 10, 1994. The dinner featured an owner-manager of a winery in Oregon. She requested that her own wine be tasted at the dinner. The wine was not yet listed in the state but the Commission was assured that this was to be done as soon as it was available. The wine was in fact submitted for listing on March 22, 1994.

In order to accommodate the visit to New Hampshire of this vintner, the Commission charged a fee of $5.47 per bottle for three bottles. Once the submission arrived, it was calculated that the fee should have been $1.28. The commission charged over four times the amount that it ordinarily would have charged.

In 1992, the Commission's Enforcement Division had received information which led to the conclusion that an unlicensed vendor representative had tasted unlisted wines in private homes in the seacoast area, which had resulted in private citizen orders being placed in our retail stores under Liq. 306.03. On May 26, 1992, the citizen in question met with our Assistant Chief of Enforcement. The citizen was told to: 1) obtain a license to solicit in the state and, 2) 'cease and desist' this practice. The vendor was not fined because she was not licensed. No other reports of this type of activity have been received to date, and she is now licensed. The LBA observation was therefore, unfounded and in fact, the date referred to was inaccurate.

At the present time, there are no administrative rules covering the area of wine-tastings. As the need for wine-tasting, as a marketing and educational tool increases, the Commission will be faced with requests to utilize wine-tastings as part of a balanced marketing program. Therefore, we requested the Legislature to add an amendment to House Bill 144 (regarding liquor tastings / so that we could write regulations regarding both liquor and wine tastings.

There already is a process in place to account for wines withdrawn by vendor representatives from their bailment accounts for use in wine-tastings.

Wine-tastings are required to be held in a licensed premise, if not, a one-day license must be obtained.

As the state becomes recognized as a premium wine market, wine-makers, winery owners and nationally recognized wine writers will be attracted to our state to present and discuss premium wines. These presentations may occasionally require the use of wines for comparison purposes that are not registered in the state due to their limited supply. Provided that the Commission determines, on an individual basis, that the intent of these presentations is to promote premium wines in general and not to promote specific bottles for future sale, these presentations should be supported as a valuable marketing tool. However, the state should be compensated for the temporary use of these limited wines which are not registered in the state.

OBSERVATION NO. 44 (Continued)

LBA REBUTTAL:

RSA 541-A is clear. Rules are required when agencies prescribe procedures binding on persons outside the agency, as in the bailment operation. The SLC's assertion that no complaints have been filed by vendors is irrelevant, as is the SLC's assertion that policies and procedures allow it "to operate efficiently in a dynamic business environment."

According to staff for the administrative rules committee, the commissioners made statements regarding qualities "recognized" by the committee. The committee did not take any action to affirmatively "recognize" any SLC qualities. Administrative rules committee staff also stated that if the 10-day order is used consistently then a formal rule would be preferable to an order.

OBSERVATION NO. 45

COOPERATIVE ADVERTISING

AUDITEE RESPONSE:

We do not concur with the observation of the Legislative Budget Assistant Audit Division (LBA) with respect to the cooperative advertising.

The advertisements referred to the LBA are placed independently by liquor and wine distillers and brokers. The Commission offers no inducement, nor does it pay or otherwise compensate distillers or brokers with respect to these advertisements.

The Commission determines which items will be placed on sale and at what price. Then we notify the vendors, primarily to ensure adequate inventory levels are available. The vendor independently decides if they wish to advertise their products. Whether or not they advertise has no bearing on the product selection. Accordingly, there is no inducement by vendors to the SLC to purchase these products.

The Commission does, in fact, purchase a small space advertisement, which is placed by the newspapers, at the bottom of each full-page advertisement. Newspaper readers can clearly note the statement placed above the Commission space which reads that the advertisements above are ..."place and paid for by individual liquor distillers, not the State Liquor Commission."

The LBA inaccurately states in its observation that the Commission..."approves the advertisements before they appear". This statement is both false and misleading.

The Commission receives a proof copy of the advertisement prior to printing. A Commission staff member in marketing proofs the ad only to ensure product prices and product code numbers are correct. This review is done as a professional courtesy for the newspapers. By reviewing the accuracy of prices and codes, the Commission prevents consumer confusion resulting from possible publication errors. Other than the price and product code proofing, the Commission offers no comment, approval, or disapproval with respect to this type of advertising.

The Bureau of Alcohol, Tobacco and Firearms' (BATF) regulation, with respect to cooperative advertising, is designed to prevent any inducement, collusion, or exclusion of products. Clearly, the Commission has not violated any BATF rule or other federal regulation with respect to this advertising. Moreover, we find the LBA observation to be in direct contradiction with all federal agencies which regulate the Commission with respect to this issue. Most importantly, to our knowledge, neither the BATF or any other federal agency has ever questioned the appropriateness referred to by the LBA.

OBSERVATION NO. 45 (Continued)

While the Commission's small ad may give the appearance to the casual observer that it is part of the remaining page of individual advertisements sponsored by others, this does not mean the Commission has violated any federal regulation.

Finally, the LBA refers to proposed BATF rule-making with respect to this issue and it states that the Commission..."will be engaging in and benefiting from cooperative advertising with liquor industry members in violation of the FAA". This LBA statement engages in speculation that this proposed rule will in fact be enacted and further presupposes that the Commission would then choose to blatantly ignore any newly enacted regulation.

The Commission adheres to all BATF rules and regulations and would certainly act to conform to any changing regulations.

LBA REBUTTAL:

If the SLC does not "approve" these advertisements how does the agency ensure compliance with RSA 175:4 and administrative rule Liq 401.02 "Prior Approval of Commission?"

Contacts with BATF indicate sections of the proposed rules pertinent to the type of advertising cited in our observation will be enacted. Our intention was to alert the SLC of this change.

OBSERVATION NO. 46

CLARIFICATION OF RSA 175:4, ADVERTISING

AUDITEE RESPONSE:

We do not concur with the observation of the Legislative Budget Assistant Audit Division (LBA) with respect to the advertising issue.

The LBA's Observation No. 46 refers to the advertising placed in New Hampshire newspapers which is also addressed in Observation No. 45.

The LBA inaccurately states in its observation that the Commission..."By cooperating with industry members in placing significant amounts of advertising in in-state newspapers, the Commission is knowingly exceeding legislative intent to limit in-state advertising expenditures."

As we previously noted, the advertisements referred to by the LBA are placed independently by liquor and wine distillers and brokers. The Commission does, in fact, purchase a small space advertisement, which is placed by the newspapers, at the bottom of each full-page advertisement. Newspaper readers can clearly note the statement placed above the Commission space which reads that the advertisements above are..."placed and paid for by individual liquor distillers, not the State Liquor Commission."

It should be noted that it is a highly acceptable practice, in advertising, to group related products and retail outlets in certain types of special advertising promotions. Simply because the Commission exercises sound marketing acumen by having its small advertisements placed at the bottom on industry-sponsored ads, does not mean it is cooperating, sponsoring, or is in any other way involved in a collusive, inappropriate, or illegal advertising effort.

Further and most importantly, the Bureau of Alcohol, Tobacco, and Firearms (BATF), which has strict regulations regarding cooperative advertising, has never raised an objection to New Hampshire Liquor Commission advertising. The BATF does not view the Commission's actions with respect to this issue as..."cooperating with industry members in placing significant amounts of advertising..." as asserted by the LBA.

The LBA refers to "legislative discussions" as a means of interpreting legislative intent regarding this issue. New Hampshire law is quite clear with respect to advertising expenditures; it requires that the Commission spend no more than 20% of its media advertising within state borders.

The LBA reviewed all Commission expenditures for advertising and found that it had complied fully with this requirement. However, the LBA attempts to link independent industry sponsored advertising to the Commission itself in its claim of possible violations of so-called "legislative intent".

OBSERVATION NO. 46 (Continued)

Certainly, the legislature did not intend to ban or otherwise prohibit distillers and manufacturers from advertising their products. Had this been the legislative intent, the General Court would have simply enacted legislation which would have accomplished this objective. The legislature chose to give authority to the Commission to regulate such advertising, not in an effort to eliminate it, but rather to insure it was conducted in a tasteful and socially acceptable manner.

Members of the legislature are well aware of the significant advertising undertaken by the spirits and wine industry. No legislative objection has ever been raised with respect to these advertisements paid for and placed by private industry. No legislation has ever been introduced which would ban these advertisements or otherwise restrict their placement.

The legislature's action, with respect to placing a limit on in-state advertising, is clearly confined to state funds and in no way was intended to limit advertising paid and placed for by the private sector.

Finally, after having said all of that, the Liquor Commission in reviewing the preliminary work sheet observed, for the first time, the same problem that LBA discovered with the current wording of RSA 175:4.

During the 1990 recodification, in the sub-committee work session, it was determined by the sub-committee that the former RSA 175:10 **Advertising** should be rearranged so that the former RSA 175:10, II prohibiting any advertising, unless it was approved by the Commission, would come first.

During the recodification process, neither the sub-committee, full-committee, the Liquor Commission or legislative bill writing noticed that the cite in section III referring to the former section I needed to be changed to II to make the proper reference. We enclose a copy of the former laws prior to recodification and after recodification to make our point.

After checking with our representatives who worked with the sub-committee, we find there was no intent on any one's part to change the intent of the law from what it read prior to recodification. The focus of a recodification is to order and not create substantial change in the law. Even when the statute was amended in 1991 no one noticed the cite was incorrect.

As you noted, before recodification the cite referred to the fact that the Liquor Commission was **"authorized to advertise...liquor and beverages** through the medium of newspapers" et. al. Section III referred to advertising by the Commission with regard to appropriations (made by the legislature in that no one else appropriates money for the Commission).

Legislation has been introduced to correct the cite in section III so that the proper reference is made as there was never an intent to change the law during recodification.

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DEPARTMENT OF JUSTICE
STATE OF NEW HAMPSHIRE
33 CAPITOL STREET
CONCORD, NEW HAMPSHIRE 03301-6397

JEFFREY R. HOWARD
ATTORNEY GENERAL

GEORGE DANA BISBEE
DEPUTY ATTORNEY GENERAL

March 31, 1995

Michael L. Buckley, CPA
Director of Audit
LBA Audit Division
State House, Room 102
Concord, New Hampshire 03301

Re: State Liquor Commission Performance Audit

Dear Mr. Buckley:

In the course of the Legislative Budget Assistant's (LBA) performance audit review of the State Liquor Commission (SLC), you referred a number of issues to us for review and possible independent investigation. We have consulted with the Chairman of the SLC, advising him of our independent review, have interviewed relevant parties and witnesses, and have measured our findings against appropriate legal standards.

Our overall conclusion is that, while the observations in question relate to specific incidents, rather than a pattern of conduct, the issues raised are substantial. Some of the observations address SLC actions taken under unclear or nonexistent policies and procedures, subjecting those actions to criticism that could have been avoided. Other observations address violations of known policies and procedures. In some instances, the actions of the SLC are in retrospect understandable and defensible; however, public and legislative confidence in the SLC will be maintained only if there is careful attention to and strict compliance with appropriate state policies. We will be working with the SLC, pursuant to RSA 7:8, to make the changes that are called for. Our specific responses to the observation worksheets follow.

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Observation #21 questions whether or not funds appropriated for an advertising contract were used for non-advertising purposes. The observation states that the State Liquor Commission authorized the diversion of $30,000 from the advertising contract appropriation to develop a shelf management program. It is also stated that the SLC expended approximately $9,000 in funds from the advertising contract to pay for production, contest award winners, and prizes for store employees, in a program called the "Golden Knife Award". The question raised is whether the SLC Commissioners have violated the provisions of RSA 9:19, which prohibits the expenditure of funds for unauthorized purposes. Our review of this issue determined that there was confusion and ambiguity concerning the meaning of the term advertising. The SLC notes that the term can incorporate merchandising along with what would commonly be recognized as traditional advertising. Given the ambiguity of the term advertising, we cannot say that the SLC Commissioners violated the provisions of RSA 9:19. However, to adopt the SLC's interpretation would appear to permit very broad expenditures that have not been considered by the Legislature or the Governor and Council. Any future advertising contract should make clear what is meant by that term.

Observation #29 asked us to determine whether or not preferential treatment was given to a local liquor manufacturer by the SLC. Our investigation determined that a local liquor manufacturer was allowed to store merchandise in the state liquor warehouse without paying a bailment charge that was charged to all other manufacturers. It is our determination that the SLC did not violate any state or federal laws, and that the disparate treatment appears to have been rationally based. However, in the absence of clear guidelines accessible to all, this disparate treatment, at a minimum, creates an appearance of arbitrariness. The SLC should adopt a written policy concerning bailment charges and apply the policy equally to all manufacturers.

Observations #22, 23, 24, and 25 all deal with an agreement between an advertising company and the SLC's MIS Director to develop for the SLC an information system for shelf management. The advertising company was authorized to enter into this agreement pursuant to a letter from the SLC. However, the terms of the contract between the advertising company and the SLC prohibited the employment of state employees. The agreement with the MIS Director therefore required an amendment to the contract, approved by the Governor and Council. No amendment was prepared and approval was not obtained.

We reviewed whether the SLC Commissioners or the MIS Director violated the provisions of RSA 95:1, relating to conflicts of interest in the purchase of goods or personal property. It is our determination that there was no violation of RSA 95:1 because there was no contract to sell goods or personal property to the State. The arrangement with the MIS Director appears to have been in the nature of a personal services contract. Accordingly, it does not fall within the provisions of RSA 95:1. However, because there was no written contract, we cannot determine definitively what provisions were in place for any product developed, or the ultimate ownership of such product. Nor were we able to determine whether prior approval of the Director of the Office of Information Technology Management was required. <u>See</u> RSA 21-I:11(Xl, Xll), although we note that ordinarily such approval would be required. Had this procurement been accomplished using regular state procedures, none of these questions would remain.

Observation #26 presents the issue of whether or not the SLC Commissioners complied with state purchasing requirements in purchasing woodworking equipment, office windows, and carpeting. We found that employees of the SLC issued purchase orders for under $1,000 to pay for purchases of goods that amounted to over $2,000. The practice of stacking purchase orders in order to avoid the requirements of RSA 21-I:11 and RSA 4:15 is not permitted. The SLC should have followed the provisions of RSA 21-I:11 and solicited bids for the goods it wished to purchase. We have no reason to believe this was other than an isolated incident, nor that there was improper personal gain or other impropriety.

Observations #27 and 28 concern compliance with state laws regarding temporary and part-time employees. We found that the SLC permitted an employee who was hired to work 20 hours per week to work 40 hours per week for more than six months so that that employee could receive health and dental benefits. This was done without the approval of either the Division of Personnel or the Department of Administrative Services as required by policy implemented pursuant to RSA 98-A:6-a. We also found that there was an attempt to create a permanent full-time position for the part-time employee in question. This was done despite the fact that Chapter 261:1, Laws of 1990, required agencies with open full-time positions to hire the first qualified person previously laid off from state service. This attempt to create a full-time position to hire one employee who had not been previously laid off appears to have been an action that was not in compliance with RSA 21-I:52(I), which prohibits any person from using any official authority or influence to secure or attempt to secure for any person an appointment or advantage in appointment to a position in the classified service for any political or other consideration.

Finally, we conducted interviews to determine whether any other state officials interceded in this matter. We determined that, as a result of an inquiry to the Governor's Office, a staff member of that office inquired of the SLC and the Department of Administrative Services whether the part-time employee was permitted to remain in full-time status. Both the

SLC and the Department of Administrative Services advised that personnel regulations would not permit that status to remain. No further action was taken; we therefore conclude that the inquiries were not improper.

We are willing to discuss this letter and our responses to your observations with you at any time. Please let us know if you have any additional questions.

Very truly yours,

Daniel J. Mullen
Chief of Staff

DJM/p

cc: Joseph Acorace, Chairman
Anthony Maiola, Commissioner
Miriam Luce, Commissioner