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State Auditor

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Members of the Legislative Audit Committee:

The Alcoholic Beverage Commission (Commission) issues most new licenses and permits in a timely manner. Errors made by field offices delay some new licenses, but our testing showed that the Commission issued 73.2 percent of the 138 new licenses we tested (in 14 days or less.) New licenses enable new businesses to generate jobs and tax revenue. The Commission prioritizes new licenses over renewals because businesses can still operate while awaiting a renewal. This prioritization has created a two-month backlog for license renewals. The renewal backlog causes the State to lose interest on beer license renewal fees because these fees are paid to local county tax assessors; the Commission bills the county after a license is issued. (All other renewal fees are paid directly to the Commission.) As of February 2002, approximately \$712,000 in beer license renewal fees awaited processing.

The Commission's performance measures do not reflect the time it takes to actually issue new licenses. The definition for "Percent of Original License/Permit Applications Processed Within 14 Days" counts an application as processed when the license is issued or when the central office requests more information from a field office or applicant. According to the definition, the Commission exceeded its fiscal year 2001 target of processing 95 percent of new licenses within 14 days. As noted above, our testing of 138 new licenses found that the Commission actually issued 73.2 percent in 14 days or less. The Commission does not have a performance measure for the time it takes to renew a license.

We also found that information about applicants, licensees, and applications is not readily available for staff members' use or management decision-making. The Commission's automated system contains accurate information, but its ability to produce data in a useful and timely manner is limited.

The Commission collects and processes revenues from new licenses, liquor license renewals, and enforcement penalties accurately and promptly. Furthermore, the Commission has good controls over the storage and sale or destruction of seized assets.

The attachment to this letter contains detailed findings and the Commission's response. The Commission agrees with our recommendations. If you have questions, contact Julie Ivie, Audit Manager, at (512) 936-9500.

Sincerely,

Lawrence F. Alwin, CPA
State Auditor

ejm/Attachment

cc: Chairman and Commissioners, Texas Alcoholic Beverage Commission
Mr. Rolando Garza, Administrator

An Audit Report on Licensing and Enforcement at the Alcoholic Beverage Commission

Alcoholic Beverage Commission

The Commission is responsible for licensing the alcoholic beverage industry and for enforcing the Alcoholic Beverage Code.

In fiscal year 2001 the Commission collected approximately \$197.6 million in state revenues. This amount includes revenues from licenses, fees, penalties, and taxes on alcohol and cigarettes crossing the border from Mexico. The Commission's appropriation for the 2000-2001 biennium was approximately \$25 million per year.

The Commission issues 62 different types of licenses. In fiscal year 2001 it issued 93,400 licenses and conducted 97,063 inspections. The Commission was allocated 527.5 full-time equivalent employees (FTE) for the 2000-2001 biennium. Thirty-nine of these authorized FTEs were licensing processors.



Most New Licenses Are Issued in a Timely Manner, But Backlogs Exist in Issuing Renewal Licenses

The Alcoholic Beverage Commission (Commission) issues most new licenses in a timely manner, but it has a two-month backlog in issuing renewal licenses. The Commission makes new licenses a priority because they generate new jobs and tax revenue for the State. Our testing of licenses issued and renewed during fiscal year 2001 revealed the following:

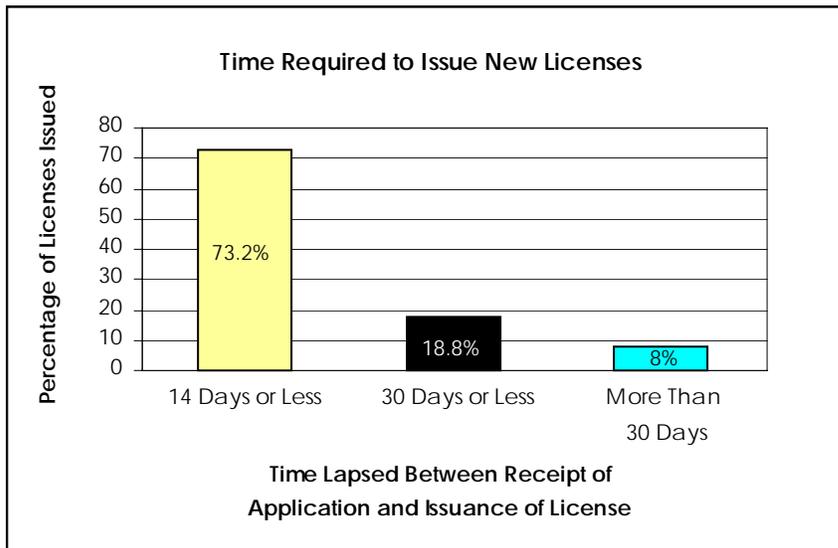
- Of 138 new licenses issued in fiscal year 2001, the Commission issued 73.2 percent in 14 days or less (see Figure 1). The performance data we reviewed from other states indicated that California processes new licenses in 45 to 60 days, Florida in no more than 90 days, and Arizona in 65 to 105 days.
- We tested 137 liquor and beer renewal licenses issued in fiscal year 2001, and found that it took an average of 67 days for these renewal licenses to be issued. As of February 6, 2002, the licensing processors were processing renewal applications received on December 10, 2001.

Businesses can operate while awaiting a renewal, and for all licenses except beer licenses, businesses pay their fees to the Commission when they apply for a license. For beer licenses, businesses pay the fee to their county, and the Commission bills the

county after issuing the license. Therefore, the renewal backlog delays the receipt of funds and causes the State to lose interest on beer license renewal fees. As of February 2002, 4,315 beer license renewals were awaiting processing. These renewals represent \$712,074 in uncollected fees.

Errors made by the Commission's field offices contribute to the application processing delays. Businesses

Figure 1



Source: State Auditor's Office testing of Commission files

submit the majority of applications for new licenses to Commission field offices, which are responsible for ensuring that the applications are complete before forwarding them to the central office for processing. When the central office receives an incomplete application, Licensing and Compliance Division (Licensing) staff must resolve the issue, which takes time away from license processing. According to Commission reports, 51 percent of applications submitted by field offices in fiscal

year 2001 were incomplete. Between September 2001 and February 2002, 53 percent were incomplete.

The Enforcement Division, not Licensing, oversees field office account examiners who review and process licenses. This organizational crossover makes it difficult for

The Commission Uses a Manual Licensing Process

The licensing process at the Commission is highly paper-intensive. Applicants must complete their applications on paper and submit them by mail after field office review. The Commission relies on paper files for detailed information on its 74,549 licensees. (As reported by the Commission.)

Licensing to resolve issues or hold the field office staff who forward incomplete applications accountable. Licensing provides training and checklists to the field office account examiners, but Enforcement Division management must resolve any significant problems.

Staff turnover in Licensing also may have contributed to the delays in processing applications. The Commission reports that its central office Licensing staff consists of 39 authorized full-time equivalent positions. Twenty-two licensing staff resigned or were terminated in fiscal year 2001, according to the Commission. (This includes 10 part-time or temporary staff.)

The Commission reports having taken steps to address the turnover in licensing processors. It reclassified these positions in December 2001. As a result of the reclassification, salaries were increased. With these changes, the Commission hopes to reduce staff turnover and improve morale.

Recommendations:

The Commission should:

- Determine the relative priority of processing beer renewal applications to prevent interest from being lost on fees received from county tax assessors.
- Consider moving field office account examiners under the Licensing and Compliance Division rather than the Enforcement Division. A Licensing supervisor in each region could provide supervision, training, and support.
- Develop a tool, such as an automated daily report, to monitor the number of renewal applications pending review by a processor. This would provide the Commission a more accurate idea of the number of outstanding renewal applications and provide management the opportunity to prioritize the work and adjust workloads as necessary.
- Consider designating one correspondence staff person to immediately address all minor issues on renewal applications that prevent a renewal license from being issued. This would expedite the process and ultimately allow the Commission to bill counties and collect fees sooner.

Management's Response:

- *Prioritization will be immediately implemented by the Licensing Department Director with beer licenses fees being one of the determining factors. Licensing currently operates on a first-in-first-out priority and if processing beer licenses is*

always the priority, liquor permits will continually be pushed farther and farther behind. It is anticipated that, when fully staffed, this will not be an issue.

- *This has been considered in the past and the Administrator and Assistant Administrator will continue to evaluate moving field office account examiners under the Licensing and Compliance Division. One issue to consider is the fact that seventy-three percent of the field offices that process applications do not have full time accounts examiners and must rely on personnel who also have other duties unrelated to processing applications. Also, the Chief of the Enforcement Division will be responsible for ensuring improvement of the error rate. Such improvement should occur immediately and be ongoing.*
- *We agree an automated report might be a helpful tool and the automated report would help in eliminating the manual effort in counting renewals. The Licensing Department Director on or before May 1, 2002 will request such a report.*
- *We concur with the recommendation. It has always been the practice of the department to have one employee to focus on renewals. With the return of the correspondence supervisor from extended sick leave and the addition of one additional FTE in the customer service section, the correspondence should remain current. The Licensing Department Director will be responsible for monitoring this recommendation and improvement should occur immediately and be ongoing.*

Section 2:

Performance Information About Licensing Does Not Reflect Backlogs

Performance information on issued licenses may be misleading:

Permits Versus Licenses

The Commission issues permits for liquor activities and licenses for beer activities. We used the generic term "licenses" to refer to both liquor permits and beer licenses.

- The Commission's performance measure for the number of new licenses processed within 14 days includes licenses actually issued and applications that are incomplete or contain errors. The definition allows the Commission to count incomplete and incorrect applications as processed once the Commission notifies the applicant and/or the field office of the problem. It may actually take much longer for the problem to be resolved and the license issued. According to the definition, the Commission exceeded its fiscal year 2001 target of processing 95 percent of new licenses within 14 days. We tested 138 new licenses issued in fiscal year 2001 and found that the Commission actually issued 73.2 percent in 14 days or less.
- The Commission does not have a performance measure that captures the time it takes to process a renewal license. As discussed in Section 1, we tested 137 renewal licenses issued in fiscal year 2001 and found that it took an average of 67 days to issue these renewal licenses.

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Recommendations:

The Commission should:

- Work with the Legislative Budget Board to develop a performance measure definition for new licenses processed that fully captures the time it takes to issue new licenses.
- Work with the Legislative Budget Board to develop a performance measure for the processing of renewal applications.

Management's Response:

- *As part of the strategic planning process, the agency will continue to work closely with the Governor's Office and the Legislative Budget Board to review performance measures including a measure definition for new licenses processed that fully captures the time it take to issue new licenses.*
- *As part of the strategic planning process, the agency will continue to work closely with the Governor's Office and the Legislative Budget Board to review performance measures including a performance measure for the processing of renewal applications.*

Section 3:

The Available Information Technology Limits Information Needed for Management Decision-Making

The Commission's automated information is accurate with only minor exceptions, but it is not readily available for management decision-making. Some automated information is available on the Commission's Model 204 (M204) database system, but the system is limited in its ability to compile timely information, and it cannot track the location of licensing files as they are being processed.

The Commission's Controls Over Physical Security, System Access, and Computer Operations Are Adequate

A recent contracted internal audit report, "Texas Alcoholic Beverage Commission Internal Audit of the Information Resources Department" (February 25, 2002) found that the Commission has implemented:

- Adequate internal controls over computer operations
- Access control measures
- Physical security measures over automated resources
- Adequate internal controls over hardware and software acquisitions
- Effective procedures for monitoring software use

The M204 system cannot easily produce management reports. Special report requests must be programmed into the M204 system. These reports are difficult to analyze because of the way they are presented. Information is entered into the system and batch-processed at night. This makes it impossible for the Commission to have timely and user-friendly management information available.

For example, the Commission tracks the number of incomplete applications and the number of errors on each application for applications reviewed by its field offices. This information is entered into the

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M204 system and reports are produced. These reports are not used regularly by management to determine where problems exist in the field office review process. We evaluated these reports for fiscal years 2001-2002 and found that they were not presented in a way that made it easy to compare performance between regions or between offices within regions. It was necessary to enter them into a spreadsheet in order to make these comparisons.

In fiscal year 2001, the Commission received approval from the Legislative Budget Board via its biennial operating plan (BOP) to replace its M204 system, but funds were not appropriated to cover the expense. The cost of replacing this system with a web-based client server system was estimated at \$4.1 million during the 2002-2003 biennium. However, the Commission estimates that it would save approximately \$119,000 in annual operating costs by moving to a web-based system. The agency also expects to improve its customer service by being able to provide up-to-date information to the Commission and the public.

There are some steps that the Commission could take in order to begin automating the licensing process and to improve efficiency. For example, the processing of a license requires action by several different staff members in the central office. When one of them needs to check on an application in progress, he or she must walk around the office and physically search for the licensing file. A card checkout system is used for existing files, but it does not indicate the file's location as it is being processed. This makes it difficult and time-consuming to provide licensing status information to licensees. An imaging system or bar-coding system would enable staff to have easier access to licensing files.

Recommendations:

- The Commission should improve and use its existing reports and develop new methods to track the number of incomplete and incorrect applications received from field offices. This would enable management to identify the field offices having problems and provide additional training or assistance as needed.
- The Commission should evaluate the possibility of moving to an imaging system or bar-coding system as a first step toward automating the licensing process. This would make it easier for licensing staff to locate files being worked.
- The Commission should pursue its goal of replacing its legacy M204 database system when funding becomes available.

Management's Response:

- *The agency concurs with this recommendation. The current reports were designed for individual districts' use and not an overall management report. The report will be expanded for headquarters and management use. The Licensing Department Director and the Assistant Chief of Enforcement will be responsible for ensuring the report is produced by May 1, 2002.*

- *The agency has evaluated several different systems in the past: however, funding has always been a key issue regarding implementation and acquisition. During the current biennium and the upcoming legislative appropriation request process, we will explore the use and cost of the imaging system and review our current card system. The Licensing Department Director and the Information Resources Department Director will be responsible for the evaluation.*
- *The agency concurs with this recommendation and plans to continue pursuing its well-documented strategy of re-engineering the legacy database systems with modern technology. During the strategic planning process, this key strategy will be reworked to determine the most realistic implementation approach for the next legislative session. The agency anticipates revising the project implementation schedule and subsequent funding request so that the development costs are allocated over multiple funding periods. The Administrator and Assistant Administrator will be responsible for implementing this recommendation with an expected completion date at the end of the next legislative session or when the legacy database system is replaced.*

Section 4:

Revenue Processing Results in Accurate and Timely Deposits

The Commission has an accurate and timely system for collecting revenue generated from new licenses, liquor license renewals, and enforcement penalties. Revenues from beer license renewals are collected as soon as the licenses are issued, although there are some backlogs in issuing these licenses. (See Section 1.) The Commission generally deposits funds within three business days as required by state law. The Commission collects and deposits funds from enforcement penalties and from the sale of seized assets when the penalty or sale is final. County tax assessors are billed monthly for the beer licenses that were issued during the prior month. The Commission ensures that counties pay these bills promptly.

The Commission is authorized to sell seized assets such as unopened liquor bottles and empty beer kegs. These sales accounted for \$89,539 in funds for General Revenue in fiscal year 2001. We reviewed all of the reports of sales for fiscal year 2001 and did not find any errors.

Fines are levied for violations of the Alcoholic Beverage Code. The Commission collected \$2.4 million in funds for General Revenue in fiscal year 2001. We reviewed all of these transactions for fiscal year 2001 and followed a sample of 30 of these transactions through the revenue process. We found that they were all collected as required.

Fees for beer licenses are paid to local county tax assessors. The Commission bills the county tax assessor each month for licenses issued during the previous month, less five percent retained by the county. We observed the tax assessor billing process for January 2002 and tested a sample of bills from fiscal years 2001 and 2002. We found that the billing and collection of these payments resulted in the accurate and timely collection of these revenues.

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Section 5:

The Enforcement Division Ensures Licensed Establishments Are Inspected Regularly

The Enforcement Division has an adequate system for ensuring that the majority of licensed establishments are inspected annually. We reviewed the method used to assign and document routine inspections and found that these methods were sufficient to ensure that licensees are inspected regularly. The results of a trend analysis indicated that enforcement officers spend an appropriate amount of time on inspections. We compared penalties assessed by the Enforcement Division to the Commission's penalty charts and did not find any errors.

The field offices provide inspectors with lists of establishments that have not been inspected within the past year in order to ensure that they meet their performance measure "*Percentage of Licensed Establishments Inspected.*" The goal for this measure is 70 percent, and the Commission reports that it inspected 67.8 percent of licensed establishments in fiscal year 2001.

Section 6:

Accountability For Seized Assets Is Sufficient

The Commission is responsible for maintaining seized assets as evidence in enforcement actions, and then destroying or selling seized alcohol when the enforcement action cases are closed. We found that the Commission had good controls over the storage and sale or destruction of seized assets. We reviewed the revenues from seized assets and found that the funds from the sale of these assets were deposited into General Revenue as required.

- We reviewed the monthly Confiscated Liquor Reports for fiscal year 2001 and found no problems.
- We tested seized assets in the Austin field office and found that all assets were accounted for and, with some minor exceptions, were properly stored and maintained. Destruction was documented and witnessed appropriately.

Summary of Objectives, Scope, and Methodology

Our objectives were to determine if the Commission:

- Has an efficient method of processing and issuing alcoholic beverage licenses and permits.
- Properly ensures that it detects violations of the Alcoholic Beverage Code.
- Safeguards seized property and assets.
- Produces accurate and reliable licensing and enforcement information.

We reviewed and tested the business process control structure for the Commission's Licensing Department and Enforcement Division and identified strengths and weaknesses. We reviewed and tested the controls over seized assets. In addition, we reviewed work performed by the contracted Internal Auditor in the accounting and information technology areas.

Our work was performed between October 2001 and February 2002. This audit was conducted in accordance with generally accepted government auditing standards.