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An Audit Report on

# **The Alcoholic Beverage Commission's Excise Tax Collection Process**

October 2009

Report No. 10-010



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### *Overall Conclusion*

The Alcoholic Beverage Commission (Commission) collected, accurately processed, and deposited excise taxes into the State Treasury. The Commission reported it collected \$188 million and \$194 million in excise taxes in fiscal years 2008 and 2009, respectively.

Auditors reviewed 20 of 550 monthly excise tax reports (4 percent of April 2009 reports) that wholesalers and distributors filed with the Commission in April 2009 and identified no significant errors. However, the Commission lacks adequate controls to ensure that it is collecting all excise taxes due. Specifically:

- For each type of excise tax, only one Commission employee conducts the initial reviews of the monthly tax reports that wholesalers and distributors submit. The Commission does not rotate the staff performing these initial desk reviews.
- Supervisory reviews are conducted only on tax reports in which the initial reviewer identified an error. No supervisory reviews are performed on tax reports without identified errors.
- All invoices, shipping reports, and other supporting documentation for tax reports that do not contain an identified error are discarded.

The Commission's Compliance Audit Division generally ensured that distributors and wholesalers correctly calculated excise tax amounts due and that excise tax audit files included required documentation. However, due to limitations within the Compliance Audit Division's audit tracking system and lack of written policies and procedures, the Commission cannot ensure that it provides sufficient oversight of regional excise tax audit offices.

#### **Background Information**

The Alcoholic Beverage Commission (Commission) assesses and collects excise taxes on beer, distilled spirits, wine, and malt liquor from wholesalers and distributors. There were 140 distributors and 309 wholesalers operating in Texas in fiscal year 2008, and there were 136 distributors and 311 wholesalers in fiscal year 2009, according to the Commission's data.

Seventy-five percent of excise tax revenues are credited to the General Revenue Fund and the remainder goes to fund public education.

The Commission's Compliance Audit Division audits excise tax accounts to ensure that wholesalers and distributors comply with requirements regarding the calculation and payment of excise taxes as outlined in the Texas Alcoholic Beverage Code and the Texas Administrative Code. According to information provided by the Commission, the Compliance Audit Division audited approximately 84 accounts in fiscal year 2008 and 44 accounts in fiscal year 2009 through June 25, 2009.

## ***Key Points***

**The Commission collected, accurately processed, and deposited excise tax revenues into the State Treasury.**

Auditors tested approximately 9 percent of the excise tax payments the Commission received for February 2008 and February 2009 and determined that those payments were processed accurately and deposited in the State Treasury. Additionally, the Commission substantially complied with the three-day deposit rule.

**The Commission lacks adequate controls to ensure that it is collecting all excise taxes due.**

The Commission conducts supervisory reviews only on excise tax reports in which the initial reviewer identifies an error. No supervisory reviews are performed on tax reports without identified errors. Furthermore, the Commission does not ensure that the supervisory reviews are documented.

**The Commission's audit process provides general assurance that excise tax amounts are accurate.**

Commission procedures require regional field auditors to calculate the alcohol inventory at the distributors and wholesalers for each month and verify that the wholesalers and distributors paid the correct amount of excise taxes for a selected audit period. However, the Commission does not ensure that the regional field auditors consistently follow those procedures.

**The Commission did not provide sufficient oversight of its regional excise tax audit divisions.**

The Commission did not have documented policies and procedures for its regional excise tax divisions to use when determining which distributors and wholesalers to audit. Additionally, the Commission lacked (1) approved, written procedures for conducting Ports of Entry Bridge Excise Tax audits and (2) policies and procedures that identify and document training requirements for its regional field auditors.

**The Commission lacked sufficient controls to ensure that its audit tracking data is reliable and that its licensing system is secure.**

The Commission's access controls over the Audit Reporting and Tracking System (ARTS) were not sufficient to ensure the reliability of the data in that system. Additionally, the Commission lacked sufficient access and security controls over its LicenseEase system.

## ***Summary of Management's Response***

The Commission generally agrees with the findings and recommendations in this report. The Commission's management responses to the specific recommendations in this report are presented immediately following each set of recommendations in the Detailed Results section of this report.

## ***Summary of Information Technology Review***

Auditors reviewed the information technology controls over the information technology systems that the Commission uses to (1) track and manage its excise tax audits and (2) record, collect, and process excise tax payments received from distributors and wholesalers. Auditors evaluated general IT controls such as access and security. Auditors identified weaknesses in access and security controls.

## ***Summary of Objective, Scope, and Methodology***

The objective of this audit was to determine whether the Commission has processes that provide reasonable assurance that excise taxes due from wholesalers, distributors, and other suppliers of alcoholic beverages are collected for the State.

The scope of this audit covered a review of the Commission's processes, documentation, and financial information related to excise tax collection and the automated systems and processes that support the collection of excise taxes for the period from September 1, 2007, through June 30, 2009.

The audit methodology included reviewing internal controls and processes related to charging, collecting, reviewing, and auditing excise taxes paid by wholesalers, distributors, and other suppliers of alcoholic beverages; reviewing excise tax payment deposits, excise tax reports, and excise tax audits; and analyzing excise tax payment data.

Auditors communicated other, less significant issues to Commission management separately in writing.

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# Detailed Results

## Chapter 1

### ***The Commission Appropriately Recorded Excise Taxes It Collected; However, It Should Improve Its Processes to Ensure That It Collects All Taxes Due***

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The Alcoholic Beverage Commission (Commission) collected, accurately processed, and deposited excise taxes into the State Treasury. The Commission reported it collected \$188 million and \$194 million in excise taxes for fiscal years 2008 and 2009, respectively. In addition, the Commission substantially complied with the three-day deposit rule.

However, the Commission lacks adequate controls to ensure that it is collecting all taxes due. For example, supervisory reviews are conducted only on excise tax reports in which the initial reviewer identifies an error. No supervisory reviews are performed on tax reports without identified errors. Furthermore, the Commission does not ensure that the supervisory reviews are documented.

#### Chapter 1-A

### **The Commission Collected, Accurately Processed, and Deposited Excise Tax Payments**

The Commission appropriately processed all excise tax payments it received in fiscal years 2008 and 2009. Auditors tested 30 excise tax payments for February 2008 totaling \$1,056,617 (9 percent of the total \$12.3 million in excise tax payments collected in February 2008) and 30 excise tax payments for February 2009 totaling \$1,159,911 (9 percent of the total \$12.2 million in excise tax payments collected in February 2009). The Commission accurately processed and deposited all 60 payments into the State Treasury and auditors noted no errors.

In addition, the Commission appropriately processed and deposited Ports of Entry Bridge Excise Tax collections in fiscal years 2008 and 2009. Auditors tested Ports of Entry Bridge Excise Tax collections for February 2008 and February 2009 and verified that the Commission deposited into the State Treasury all Ports of Entry Bridge Excise Taxes collected for the two months tested, which totaled \$599,033.90. In addition, the Ports of Entry Bridge Excise Taxes collected at the State Treasury matched the amounts for February 2008 and February 2009, based on reports that each international bridge provided to the Commission.

Wholesalers and distributors used the correct tax rates when reporting excise taxes due in fiscal years 2008 and 2009. Wholesalers and distributors used

correct tax rates in accordance with the Texas Alcoholic Beverage Code for all 30 tax reports tested—15 from February 2008 and 15 from February 2009.

Chapter 1-B

### **The Commission Lacks Adequate Controls to Ensure That It Is Collecting All Excise Taxes Due**

The Commission receives monthly excise tax reports from wholesalers and distributors that are taxed based on the amount and type of alcoholic beverages reported depleted during the month. A Commission staff member conducts the initial review of the excise tax reports and reconciles the reports to the tax payments received to ensure that wholesalers and distributors pay the appropriate amounts. However, the Commission lacks adequate controls to ensure that it is collecting all excise taxes due. Specifically:

- The Commission does not rotate the staff performing the initial desk reviews of the excise tax reports. Four employees in the Commission's Tax Division review all excise tax reports, as well as reports submitted by manufacturers and suppliers. Each employee reviews a particular beverage type or supplier/manufacturer report.
- Supervisory reviews are conducted only on excise tax reports in which the initial reviewer identified an error. No supervisory reviews are performed on tax reports without identified errors. Furthermore, the Commission does not ensure that the supervisory reviews are documented.
- The Commission retains supporting documents only for reports in which the initial review identified a discrepancy. Employees discard supporting documents, such as envelopes with postmarks, invoices, and shipping documents, for all other excise tax reports.

Per auditors' request, the Commission retained supporting documentation for all excise tax reports it received in May 2009. Auditors reviewed 20 of the 550 tax reports received and identified no significant errors. However, because the Commission retained supporting documentation only for May 2009, auditors could not provide assurance for any other time period regarding whether:

- The Commission collected excise taxes on all purchases from and shipments to distributors and wholesalers.
- Wholesalers and distributors submitted excise tax reports on a timely basis in accordance with Texas Alcoholic Beverage Code, Section 206.07(a).
- The Commission appropriately granted bond exemptions to wholesalers and distributors in accordance with Texas Alcoholic Beverage Code, Chapter 204.

- The Commission appropriately granted 2 percent discounts to wholesalers and distributors that submitted reports on time in accordance with Texas Alcoholic Beverage Code, Section 201.06.

## Recommendations

The Commission should:

- Rotate assignments for Tax Division employees who conduct the initial reviews of excise tax reports.
- Ensure that supervisory reviews are conducted and documented for a sample of excise tax reports that includes reports with and without identified errors.
- Ensure that it retains supporting documentation for all excise tax reports for an appropriate length of time determined by Commission management to verify the accuracy and completeness of tax payments due to the State.

## Management's Response

- *The Excise Tax Section has two senior employees who review the majority of the tax reports. The other two employees are responsible for reviewing the informational reports for regulatory compliance. We will begin training the other two employees on the review process and let them begin checking a sample of tax reports each month. In addition, the agency is currently in the process of automating the excise tax reporting system which will be a more efficient process.*
- *The Excise Tax Manager currently reviews a sample of reports, but does not document the outcome. The manager will begin documenting which reports were reviewed and the review date.*
- *The Excise Tax Section will begin retaining all invoices related to each tax report for a period of three months after the month for which the report is filed.*

*Estimated completion date: January 2010*

*Title of responsible person: Excise Tax Manager*



## ***The Commission Ensured That Excise Tax Amounts Were Generally Calculated Correctly; However, It Should Increase Oversight of Regional Excise Tax Audit Offices***

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The Commission is statutorily required to audit any licensed distributor and wholesaler before it requests payment for excise taxes due (see text box). The Commission's Compliance Audit Division (Division) generally ensured that distributors and wholesalers correctly calculated excise tax amounts due and that almost all excise tax audit files included required documentation.

### **The Commission's Compliance Audit Division**

Under Texas Alcoholic Beverage Code, Section 206.08(b), the Commission must conduct audits of licensed distributors and wholesalers in accordance with national audit standards before it can request payment for excise taxes.

The Commission's Compliance Audit Division (Division) is responsible for ensuring that wholesalers and distributors are audited. The Commission has determined that the American Institute of Certified Public Accountants (AICPA) attestation standards provide the criteria best suited to its auditing function.

To manage the audits, the Commission has created five regional excise tax audit divisions. Within each region are 5 regional supervisors and approximately 54 total regional field auditors who are responsible for reviewing and conducting the audit work.

However, due to limitations within the Division's audit tracking system (see Chapter 3), a lack of sufficient documentation in the audit files, and lack of written policies and procedures, the Commission cannot ensure that it provides sufficient oversight of regional excise tax audit offices.

Chapter 2-A

### **The Commission's Compliance Audit Division Generally Ensures That Excise Tax Amounts Are Accurate**

The Commission's procedures require its regional field auditors to calculate the amounts of alcohol the distributors and wholesalers sold for each month and verify that they paid the correct amount of taxes for a selected audit period; however, testing indicates that they do not always follow these procedures. Using inventory receipts and invoices from the distributors and wholesalers, the

Commission's regional field auditors correctly verified that the amount of taxes paid were in accordance with the tax rates in Texas Alcoholic Beverage Code, Chapters 201 and 203, for 29 of the 30 audit files from March 1, 2007, to June 25, 2009, that state auditors selected to test.

In addition, the Division's *Excise Tax Audit Manual* sufficiently addressed all significant requirements in the Texas Alcoholic Beverage Code. Also, 29 of the 30 files included audit documents such as risk assessment forms, initial tax analysis schedule, and the final examination report, and the documents were completed correctly. The Commission was unable to locate 1 of the 30 excise tax audit files selected.

While the Division generally ensures that tax amounts are calculated correctly, it should make improvements to ensure that audit documentation is completed and sufficiently documented. For example, 11 of 30 audit files tested contained incomplete second level and quality control review checklists. These checklists help ensure that auditors uniformly apply audit standards as required by Texas Alcoholic Beverage Code, Section 206.08(2). Additionally, 27 of the same 30 audit files tested did not sufficiently

document the regional auditors' verifications that the total excise taxes distributors and wholesalers listed on the tax reports were correct.

### Recommendation

The Commission should ensure that regional field auditors complete audit documentation in accordance with the Commission's *Excise Tax Manual*.

### Management's Response

*The Agency concurs with the findings and agrees with the recommendations to ensure that regional field auditors complete audit documentation in accordance with the Commission's Excise Tax Manual. The division is in the process of implementing an enhanced review process of field excise tax audits. Assistant regional supervisors, or senior auditors where applicable, will conduct the second level excise tax review and the regional supervisor will complete the final excise tax review and file locally. Excise tax audits will be randomly selected for review during periodic Quality Control Field Reviews as determined by Division Management.*

*This enhanced process will emphasize the importance of complete documentation, timely review and adherence to the procedures in the Excise Tax Procedure Manual.*

*Estimated Completion - January 31, 2010*

*Title of responsible person: Assistant Chief of Compliance*

Chapter 2-B

## **The Commission Did Not Provide Sufficient Oversight of Its Regional Excise Tax Audit Divisions**

The Commission does not have documented policies and procedures for how its regional excise tax audit divisions should select which distributors and wholesalers to audit. While the Division is responsible for determining the total number of excise tax audits that each regional office will conduct each fiscal year, the regional offices are solely responsible for selecting the distributors and wholesalers to be audited. Each region uses a different methodology to select which distributors or wholesalers to audit, and the Commission does not approve the regions' selection of which entities will be audited. Use of an approved statewide audit selection methodology would help the Commission ensure that the regional offices use objective, consistent criteria when selecting distributors and wholesalers for audit.

Additionally, the Commission does not track regional offices' compliance with its internal goal that distributors and wholesalers be audited at least once every four years. Based on information from interviews with regional supervisors, most regional offices consider the amount of time since a previous audit was completed when selecting distributors and wholesalers for audit. However, the Commission does not track this information.

### Recommendation

The Commission should develop and implement standard procedures for its regional offices to use when selecting distributors and wholesalers for excise tax audits. The Commission should consider including procedures for a risk-based approach to planning audits, as recommended by the National State Auditors Association. These procedures also should include the required frequency of excise tax audits and compliance with legal and regulatory requirements.

### Management's Response

*The Agency concurs with the findings and agrees with the recommendations to develop and implement standard procedures for use when selecting distributor and wholesalers for excise tax audits. The Commission is currently creating a risk-based report that will be utilized by regional supervisors when determining excise tax audit assignments. The report will include risk-based factors including but not limited to revenue history, permit history, payment history, and audit history. The Commission will create an Excise Tax Supervisory Manual as a guide to assign and review excise tax audits. The manual will require that excise tax accounts be conducted every four years. This process will be reviewed during periodic Quality Control Field Reviews as determined by Division Management.*

*Status: Estimated Completion - March 31, 2010*

*Title of responsible person: Assistant Chief of Compliance*

## The Commission Did Not Provide Guidance or Consistently Conduct Audits of Ports of Entry Bridge Excise Tax Collections

### Ports of Entry Bridge Excise Tax

Ports of Entry Bridge Excise Taxes are payable by individuals who import alcoholic beverages and/or cigarettes for personal consumption. These taxes are primarily collected in the south and west regions of the state.

To audit the collection of Ports of Entry Bridge Excise Taxes, the Commission reviews the documentation maintained at each bridge location; it does not audit the individuals paying the taxes.

In fiscal years 2008 and 2009 (as of June 29, 2009), the Commission reported that it collected approximately \$2.3 million and \$1.7 million in Ports of Entry Bridge Excise Taxes, respectively. (See Appendix 3 for more information.)

The Commission conducted five Ports of Entry Bridge Excise Tax audits in fiscal year 2008 (see text box). As of July 24, 2009, the Commission had not conducted any Ports of Entry Bridge Excise Tax audits for fiscal year 2009. Auditors reviewed four of the five Ports of Entry Bridge Excise Tax audits from fiscal year 2008 and did not identify any significant errors in regional auditors' calculations of the amount of taxes collected.

The Commission lacked approved, written procedures for conducting Ports of Entry Bridge Excise Tax audits. In fiscal year 2008, regional offices used an audit template as a guide for conducting these types of audits. As of June 2009, the Commission drafted procedures; however, these procedures had not been finalized or implemented. Implementing approved, written policies and procedures may help the Commission ensure that these audits are conducted in a timely manner.

### Recommendation

The Commission should:

- Ensure that it conducts Ports of Entry Bridge Excise Tax audits in a timely manner.
- Develop and implement approved, written policies and procedures for its regional offices to use when conducting Ports of Entry Bridge Excise Tax audits. These policies and procedures should include guidance on the selection and approval of bridges to audit.

### Management's Response

- *The Agency concurs with the findings and agrees with the recommendations to ensure that it conducts Ports of Entry Bridge Excise Tax audits in a timely manner.*
- *Develop and implement approved written policies and procedures for its regional offices to use when conducting Ports of Entry Bridge Excise Tax Audits. In July 2009, the Ports of Entry (POE) chapter of the Excise Tax Manual was approved and completed. The division implemented these procedures on September 1, 2009. Ports of Entry Bridge Excise Tax audits will be conducted annually. To ensure POE Bridge audits are conducted timely and in accordance with written procedures, the Ports of Entry Bridge Excise Tax Audits will be randomly selected for review*

*during periodic Quality Control Field Inspections as determined by Division Management.*

*Status: Implemented*

Chapter 2-D

### **The Commission Lacks Policies and Procedures to Identify Training Requirements for Its Regional Field Auditors**

The Commission does not have written policies and procedures regarding the amount or type of excise tax audit training that its regional auditors are required to complete. The Commission also lacks procedures to ensure that it retains documentation showing the type of training each regional auditor attended and successfully completed. The Commission lacked copies of training certificates or sign-in sheets for 24 (80 percent) of 30 regional field auditors that state auditors selected for testing. Without defined training requirements and adequate documentation of training completed, the Commission cannot ensure that its regional field auditors have sufficient knowledge about the accounting and industry-specific practices required to conduct complete and accurate excise tax audits.

#### **Recommendations**

The Commission should ensure that it develops and implements written policies and procedures for:

- The amount and type of required and recommended training for regional field auditors.
- Compiling and retaining supporting documentation necessary to validate the training that regional auditors attend or complete.

#### **Management's Response**

- *The Agency concurs with the findings and agrees with the recommendations to develop and implement written policies and procedures for the amount and type of required and recommended training for field auditors. Develop and implement written policies and procedures for compiling and retaining support documentation necessary to validate the training that regional auditors attend or complete.*
- *The Compliance Division is currently working closely with the Training Division to develop and implement a program for continuing education for compliance auditors. The agency will develop procedures to ensure that all training is validated and documented by the Training Division.*

*Status: Estimated Completion - March 31, 2010*

*Title of responsible person: Assistant Chief of Compliance*

## ***The Commission Did Not Ensure That Audit Tracking Data Was Reliable or That Licensing System Data Was Secure***

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The Commission's access controls over its Audit Reporting and Tracking System (ARTS) are not sufficient to ensure that the data in that system is reliable. As a result, the Commission cannot accurately track the status of its excise tax audits of distributors and wholesalers. Additionally, the Commission lacks sufficient controls, such as proper access and security, over its LicenseEase system, which contains information about excise tax payment, license status, and other information about the Commission's licensees.

### Chapter 3-A

## **The Commission Did Not Ensure that Audit Tracking Data Was Reliable**

The Commission's access controls over ARTS were not sufficient to ensure that audit tracking data was reliable. Since April 2008, the Commission has used ARTS to track its audits of distributors and wholesalers that pay excise taxes to the State (see text box for more information about ARTS). However, the Commission has not implemented sufficient access controls over the system. For example, the Commission did not limit employee access to

### **The Audit Reporting and Tracking System (ARTS)**

Since April 2008, the Commission has used ARTS as its audit tracking system. ARTS includes audit-related information, such as audit start and end dates, dates of audit visits, amounts of tax revenues reviewed, and amounts of tax errors identified. This system is used by multiple divisions within the Commission including it Compliance, Enforcement, and Licensing divisions.

ARTS based on the access levels appropriate to each employee's job duties. A total of 533 Commission employees have full access to ARTS, which enables them to add, modify, and delete system records. While the ARTS system tracks who makes changes in the system, it does not track the type of change or what fields were changed. Also, Commission management does not review the change tracking log to identify any patterns that may indicate an employee is making inappropriate or unapproved changes.

In addition, the Commission does not ensure that audit status dates are accurate in its ARTS system. Fifty-four (25 percent) of 216 excise tax audits completed from March 1, 2007, through June 30, 2009, listed an audit completion date that was the same as or prior to the audit start date. According to the Commission, in April 2008, the Commission converted from a previous tracking system to ARTS, and some of these incorrect audit status dates were created in the previous system and not corrected during the conversion. However, 16 (30 percent) of the 54 excise tax audits with incorrect status dates were created in ARTS after April 2008.

## Recommendations

The Commission should:

- Review each employee's access to ARTS to ensure that access is appropriately limited to only the level necessary for the employee's job duties.
- Implement edit checks within ARTS that capture not only who makes changes but also what change was made and which record was affected.
- Implement a process that requires Commission management to periodically review the change tracking log and approve changes made to ARTS.
- Ensure that audit status dates within ARTS are accurate.

## Management's Response

- *The Agency agrees with the recommendation and plans to make the appropriate changes to limit ARTS access for employees to only the level necessary for the employee's job duties. These security changes will be incorporated into ARTS as part of the current Case Management project. The agency will also implement a process to ensure that management periodically reviews employee access to the appropriate system functions.*

*Estimated completion date: March 31, 2010*

*Title of responsible person: Director of Information Resources, Assistant Chief of Compliance*

- *The Agency agrees with the recommendation and plans to make the appropriate changes to implement edit checks within ARTS in order to track changes by staff person and changes to key data elements. These changes will be incorporated into ARTS during the current Case Management project.*

*Estimated completion date: March 31, 2010*

*Title of responsible person: Director of Information Resources*

- *The Agency agrees with the recommendation and plans to implement a process to ensure that management periodically reviews the change tracking log to identify any pattern that may indicate an employee is making inappropriate or unapproved changes.*

*Estimated completion date: March 31, 2010*



*Title of responsible person: Assistant Chief of Compliance*

- *A review of the audit tracking system will be incorporated into periodic Quality Control Field Reviews as determined by the Compliance Division Management. A random sampling of excise tax audits will be reviewed for accuracy and cross checked with all audit related data entered in ARTS.*
- *Effective September 1, 2009, the review process for excise tax audits has changed. All audits will now remain in the field and reviewed by the assistant and regional supervisors. This review process now includes a check of the status in ARTS. This requirement has also been added to the C-507 Regional Supervisor Review Sheet to ensure regional supervisors verify this information. In addition, several new reports have been made available for regional supervisor to track audits and their statuses.*

*Status: Estimated Completion – March 31, 2010*

Chapter 3-B

### **The Commission Does Not Adequately Limit Access within Its LicenseEase System**

While the Commission's manual processes adequately segregate duties for processing excise tax and license fee payments, improvements are needed to properly control access within its LicenseEase system. This system is used to process, manage, and record licensee information and payments (see text box). Auditors found:

#### **LicenseEase System**

The Commission uses the LicenseEase system to store and manage data about (1) entities that are licensed to sell alcoholic beverages and (2) excise tax and license fee payments that the Commission receives. While it is not the Commission's accounting system of record, the LicenseEase System is one of the key systems the Commission uses to track the various types of payments received from licensees.

Within the LicenseEase system, there are various modules, such as a license module that processes new licensee information and a cash module that allows an accounting for all cash receipts received.

- Eleven Commission employees have access rights to the cash module in LicenseEase that allow them to enter, deposit, allocate, and assign cash amounts, as well as process bad checks. While there are limited audit trails, this level of access allows each of the 11 users to fully process a cash transaction from initial batch entry to the assignment of the funds. Ten of the 11 employees with full access to the cash module also have full access to the license module. As a result, these employees could inappropriately enter a new licensee into LicenseEase and then enter and/or assign payments to that entity.
- Two of the 11 employees discussed above also have physical access to the cash and check payments before they are first entered into LicenseEase. This gives these two employees the ability to manage almost the entire cash receipts process.

According to the Commission, the majority of excise tax payments are paid using electronic funds transfers (EFT) from the distributors and wholesalers directly into the State Treasury. In fiscal year 2008, the Commission reported that it collected approximately \$188 million in excise tax payments, of which

\$175.9 million were paid by EFTs. Additionally, auditors did not identify any payments that were processed inappropriately. However, by not appropriately limiting access within the LicenseEase system, the Commission is at an increased risk that revenues will not be properly recorded.

## Recommendations

The Commission should:

- Design and implement access controls within the LicenseEase system that limit employees' access to the level that is appropriate for each employee's job needs.
- Determine whether unlimited access is required for any one user of the LicenseEase System and make adjustments to reflect this determination.

## Management's Response

- *The Agency agrees with the recommendation and has made some changes to roles to limit user access to the Cash Module of LicenseEase. The Agency plans to review and modify some business processes in order to complete the separation of duties between license creation and cash assignment.*

*Estimated completion date: January 1, 2010*

*Title of responsible person: Director of Information Resources, Director of Business Services, Director of Licensing, Director of Tax Division*

- *The Agency agrees with the recommendation and has determined that only system administrators within the Information Resources Division will need unlimited access to all LicenseEase modules. The Agency has determined that no one business user has unlimited access to the LicenseEase system.*

*Estimated completion date: October 9, 2009*

*Title of responsible person: Director of Information Resources*

Chapter 3-C

## LicenseEase Password Requirements Do Not Comply with State Information Security Standards

The LicenseEase system does not comply with the State's information security standards as documented in Title 1, Texas Administrative Code, Chapter 202, which require state agencies to use "best practices" for system

passwords. To minimize the risks related to public disclosure, auditors discussed details related to this issue directly with Commission management.

### Recommendation

The Commission should ensure that it complies with the State's information security standards as defined in Title 1, Texas Administrative Code, Chapter 202.

### Management's Response

*The Agency agrees with the finding that the LicenseEase system does not comply with state security standards. However, the Agency does comply with state password requirements for general network access which allows a user to access agency systems including LicenseEase. The agency plans to upgrade LicenseEase to Versa Regulation which incorporates information security control "best practices" for system passwords including complexity, expiration, and self-service password management.*

*Estimated completion date: August 31, 2011*

*Title of responsible person: Director of Information Resources*

#### Chapter 3-D

### The Commission Had Not Defined an Owner of the LicenseEase System

According to the Title 1, Texas Administrative Code, Section 202.21, state agencies are required to define an owner or reach a consensus on the roles and responsibilities for applications shared by more than one major business function. Owners of applications are responsible for approving and reviewing access as required by the Texas Administrative Code. Defining LicenseEase's owner can help the Commission ensure that access to the application is properly managed and that employees have access that does not exceed what is needed for their assigned job duties.

### Recommendation

The Commission should ensure that it complies with the State's information security standards as defined in Title 1, Texas Administrative Code, Chapter 202, by defining an owner for the LicenseEase system and requiring the owner to periodically review and adjust access as appropriate.

## Management's Response

*The Agency agrees with the recommendation and has designated the Licensing Division as the owner for the LicenseEase application. As owner of this system, Licensing management will be responsible for the periodic review to ensure that access to the application is properly managed and that employees have access that does not exceed what is needed for their assigned job duties.*

*Estimated completion date: October 9, 2009*

*Title of responsible person: Director of Licensing*

# Appendices

## Appendix 1

### **Objective, Scope, and Methodology**

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#### **Objective**

The objective of this audit was to determine whether the Alcoholic Beverage Commission (Commission) has processes that provide reasonable assurance that excise taxes due from wholesalers, distributors, and other suppliers of alcoholic beverages are collected for the State.

#### **Scope**

The scope of this audit covered a review of the Commission's processes, documentation, and financial information related to excise tax collection and the automated systems and processes that support the collection of excise taxes for the period from September 1, 2007, through June 30, 2009.

#### **Methodology**

The audit methodology included reviewing internal controls and processes related to charging, collecting, reviewing, and auditing excise taxes paid by wholesalers, distributors, and other suppliers of alcoholic beverages; reviewing excise tax payment deposits, excise tax reports, and excise tax audits; and analyzing excise tax payment data.

Information collected and reviewed included the following:

- Commission policies and procedures related to excise tax collection, verification, and auditing processes.
- Excise tax reports submitted to the Commission for fiscal years 2008 and 2009.
- Commission information resource security policies.
- Lists of active alcoholic beverage wholesalers and distributors for fiscal years 2008 and 2009.
- Non-filer reports generated by the Commission for fiscal years 2008 and 2009.
- Ports of Entry Bridge Excise Taxes collected during fiscal years 2008 and 2009.
- Excise tax audits conducted by the Commission's Compliance Audit Division during fiscal years 2008 and 2009.

- Audit data in the Commission’s Audit Reporting and Tracking System (ARTS).
- Excise taxes the Commission collected during fiscal years 2008 and 2009.
- Excise tax collection records in the Commission’s LicenseEase system.

Procedures and tests conducted included the following:

- Interviewed key personnel in the Commission’s Fiscal Services, Tax, and Compliance divisions to gain an understanding of the processes and controls related to the management of excise tax collections.
- Analyzed excise taxes collected to evaluate the accuracy of the Commission’s collection and deposit processes.
- Reviewed excise tax reports to verify the accuracy of tax amounts and the timely submission of tax reports.
- Reviewed excise tax audit files to ensure that audit work was conducted in accordance with the Texas Alcoholic Beverage Code and the Commission’s policies and procedures.
- Reviewed the Commission’s processes for Ports of Entry Bridge Excise Tax collections and deposits.
- Reviewed and tested the Commission’s controls over its LicenseEase system.

Criteria used included the following:

- Title 16, Texas Administrative Code, Chapter 41.
- Texas Alcoholic Beverage Code.
- The Commission’s Compliance Division’s *Excise Tax Audit Manual*.
- The Commission’s Tax Division’s *Processing Manual*.

### **Project Information**

Audit fieldwork was conducted from June 2009 through August 2009. We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

The following members of the State Auditor’s staff performed the audit:

- Courtney Ambres-Wade, CGAP (Project Manager)
- Arby Gonzales, CFE (Assistant Project Manager)
- Scott Armstrong, CGAP
- Seorin Kim, CPA
- Cain Kohutek
- Michael Yokie, CISA (Information Systems Audit Team)
- J. Scott Killingsworth, CIA, CGAP, CGFM (Quality Control Reviewer)
- Angelica C. Martinez, CPA (Audit Manager)

## ***Excise Taxes Collected by Region for Fiscal Year 2007 through Fiscal Year 2009 (as of August 15, 2009)***

The amount of excise taxes that the Alcoholic Beverage Commission (Commission) reported that it has collected has remained fairly consistent from fiscal year 2007 through August 15, 2009. Region 2 (North Region) and Region 3 (East Region) collected the most excise taxes during this time period (see Table 1).

Table 1

<b>Excise Taxes Collected by Region</b>				
<b>Fiscal Year 2007 through Fiscal Year 2009 (as of August 15, 2009)</b>				
Region	Fiscal Year 2007	Fiscal Year 2008	Fiscal Year 2009 (as of August 15, 2009)	Total Taxes Collected by Region
Region 1 - West Region <sup>a</sup>	\$ 17,289,368.99	\$ 18,084,746.26	\$ 16,762,239.20	\$ 52,136,354.45
Region 2 - North Region <sup>b</sup>	55,730,148.46	58,684,848.84	54,496,698.64	168,911,695.94
Region 3 - East Region <sup>c</sup>	48,353,870.65	50,971,327.57	49,026,163.20	148,351,361.42
Region 4 - Central Region <sup>d</sup>	29,911,723.68	31,704,193.53	29,131,284.70	90,747,201.91
Region 5 - South Region <sup>e</sup>	27,977,903.56	29,117,258.62	26,555,071.26	83,650,233.44
Outside Texas <sup>f</sup>	33,282.73	40,918.56	47,426.94	121,628.23
<b>Totals</b>	<b>\$179,296,298.07</b>	<b>\$188,603,293.38</b>	<b>\$176,018,883.94</b>	<b>\$ 543,918,475.39</b>
<sup>a</sup> Includes Lubbock, Amarillo, El Paso, Odessa, Abilene, and surrounding areas. <sup>b</sup> Includes Dallas, Fort Worth, Longview, Nacogdoches, and surrounding areas. <sup>c</sup> Includes Houston, Beaumont, Conroe, Huntsville, and surrounding areas. <sup>d</sup> Includes Austin, Waco, Victoria, New Braunfels, Brazoria, and surrounding areas. <sup>e</sup> Includes San Antonio, Corpus Christi, McAllen, Del Rio, and surrounding area. <sup>f</sup> Includes wineries outside the state of Texas.				

Source: The Alcoholic Beverage Commission's LicenseEase System.



## *Ports of Entry Bridge Excise Taxes Collected by Region for Fiscal Year 2007 through Fiscal Year 2009 (as of June 29, 2009)*

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The Alcoholic Beverage Commission (Commission) collects Ports of Entry Bridge Excise Taxes from individuals who import into Texas alcoholic beverages and/or cigarettes for personal consumption. These taxes are collected primarily along the Texas-Mexico border. As Table 2 shows, the amount of Ports of Entry Bridge Excise Taxes that the Commission collected has remained fairly consistent from fiscal year 2007 through June 29, 2009.

Table 2

Ports of Entry Bridge Excise Taxes Collected by Region <sup>a</sup>				
Fiscal Year 2007 through Fiscal Year 2009 (as of June 29, 2009)				
Region	Fiscal Year 2007	Fiscal Year 2008	Fiscal Year 2009 (as of June 29, 2009)	Total Taxes Collected by Region
Region 1 - West Region <sup>b</sup>	\$ 357,376.42	\$ 278,810.83	\$ 165,173.75	\$ 801,361.00
Region 5 - South Region <sup>c</sup>	2,385,126.27	2,023,697.57	1,535,687.50	5,944,511.34
<b>Totals</b>	<b>\$ 2,742,502.69</b>	<b>\$ 2,302,508.40</b>	<b>\$ 1,700,861.25</b>	<b>\$ 6,745,872.34</b>
<sup>a</sup> The Commission did not collect excise taxes in Regions 2 (North), 3 (East), or 4 (Central) during this time period. <sup>b</sup> Includes Lubbock, Amarillo, El Paso, Odessa, Abilene, and surrounding areas. <sup>c</sup> Includes San Antonio, Corpus Christi, McAllen, Del Rio, and surrounding areas.				

Source: Uniform State Accounting System (USAS).

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The Honorable Joe Straus III, Speaker of the House, Joint Chair  
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The Honorable Jim Pitts, House Appropriations Committee  
The Honorable Rene Oliveira, House Ways and Means Committee

### **Office of the Governor**

The Honorable Rick Perry, Governor

### **Alcoholic Beverage Commission**

Members of the Alcoholic Beverage Commission

Mr. José Cuevas, Jr., Chairman

Ms. Melinda S. Fredericks

Dr. Steven M. Weinberg

Mr. Alan Steen, Administrator



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