

FOLLOW-UP: INTERNAL AUDIT OF THE

- **FIXED ASSET MANAGEMENT**
- **TAX ADMINISTRATION – PORTS OF ENTRY**
- **INSPECTION ADMINISTRATION - COMPLIANCE**

AS OF JULY 21, 2014

AT THE

TEXAS ALCOHOLIC BEVERAGE COMMISSION

Approved by the Commission

on September 23, 2014

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Commission Members
Texas Alcoholic Beverage Commission
Austin, Texas

We have reviewed the status of our internal audit recommendations related to the following as of July 21, 2014:

- Fixed Asset Management (Report Date: January 31, 2013)
- Tax Administration – Ports of Entry (Original Report Date: March 07, 2013)
- Inspection Administration - Compliance (Original Report Date: June 05, 2013)

The accompanying schedules summarize our original findings and recommendations, current status, and remarks.

We appreciate the courtesy and cooperation shown by the management of the Agency during the course of the engagement.

Monday N. Rufus, P.C.

July 21, 2014
Austin, Texas

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Introduction and Executive Summary

In 1935, the Legislature created the Texas Alcoholic Beverage Commission (formerly the Texas Liquor Control Board).

The Texas Alcoholic Beverage Commission (Commission) is the state agency that regulates all phases of the alcoholic beverage industry in Texas. The duties of the Commission include regulating sales, taxation, importation, manufacturing, transporting, and advertising of alcoholic beverages.

The Commission collects in excess of \$200 million annually in taxes and fees from alcoholic beverage license and permit fees, alcohol beverages taxes, cigarette taxes, airline beverage tax, and revenue collected on audits. This revenue aids in the financing of the state's public schools, local governments, research, human services, and other areas in which state government provides services to all Texans and is deposited into the General Revenue Fund.

Fixed Asset Management

The General Services Section of the Commission's Business Services Division is responsible for real and personal property management which includes all fixed assets.

The Property Manager who reports to the Director of Business Services Division is the custodian of all property in the possession of the Commission and is responsible for maintaining the required records for the property. The Property Manager is also responsible for updating the Texas Comptroller of Public Accounts (State Comptroller) State Property Accounting (SPA) system records.

The Commission is considered a Reporting Status agency with its own property system set up to comply with the State Comptroller's SPA reporting requirements. State agencies which use the Comptroller's SPA system as their property system are considered to have an Internal Status.

Tax Administration – Ports of Entry

The Commission's Ports of Entry Division is charged with ensuring that persons importing alcoholic beverages and cigarettes are complying in meeting legal requirements and paying the appropriate fees and taxes under the Texas Alcoholic Beverage Code, Legislative statutes, and TABC Administrative Rules.

Ports of Entry (POE) personnel from seven (7) port Districts monitor the 28 international crossings and 2 collection locations at the Galveston port with strategically placed Tax Compliance Officers (TCO) along the Texas-Mexico border in order to maximize compliance with the personal importation laws of the State of Texas regarding alcoholic beverages and cigarettes and also to collect the appropriate fees and taxes.

The TABC also has an agreement with the Comptroller of Public Accounts which also makes the POE personnel responsible for determining compliance with the state laws in the importation of cigarettes and collecting the taxes.

Inspection Administration - Compliance

The Audit & Investigations Division has the primary responsibility of ensuring compliance with the Texas Alcoholic Beverage Code's regulatory and tax requirements under authority of the Commission by conducting inspections, a variety of audits, providing support in the initial phases of the licensing process, fee analysis, and administering education initiatives and training to permit holders and employees aimed at seeking voluntary compliance.

Internal Audit Results

The scope of this internal audit follow-up was limited to following up on the findings and recommendations included in the following:

- Fixed Asset Management (Report Date: January 31, 2013)
- Tax Administration – Ports of Entry (Original Report Date: March 07, 2013)
- Inspection Administration (Report Date: June 05, 2013)

Appendix 1 (Fixed Asset Management), *Appendix 2* (Tax Administration – Ports of Entry), and *Appendix 3* (Inspection Administration) summarize and provide the status and steps taken by the management of the Commission to the recommendations made in these reports.

Appendix 1:

ENTITY: Texas Alcoholic Beverage Commission

PROJECT: Follow-up on prior Internal Audit Recommendations – (1) Fixed Asset Management (Report

Date: January 31, 2013)

FISCAL YEAR: 2014

PRIOR FINDINGS/RECOMMENDATIONS (issued by the Internal Auditor)	CURRENT STATUS*	Brief Description of Corrective Action Taken*
<p><u>Fixed Asset Management</u></p> <p><u>Finding #1</u></p> <p>Adjust and Update the Commission’s Inventory System at the End of the Physical Inventory for Any Property Changes or Adjustments</p> <p>During our testing of inventory property we noticed forty-five (45) fixed asset items with a cost value of \$65,797.42 that had been traded in or disposed during fiscal year 2009 were still being included in the records of the MOBILE Inventory as of November 14, 2012. One of the fixed asset items was also included in the CERTIFIED Inventory which had been certified and sent to the State Comptroller’s Office at the end of the fiscal year. The fixed asset items consisted of the following:</p> <p><u>MOBILE Inventory:</u></p> <p>LAN/WAN SWITCHING – Hubs, Switches, Routers 43 \$54,571.50 OTHER OFFICE FURN(Includes modular furn./couches) 1 \$1,437.00 TELEPHONE – OTHER EQUIPMENT –CELL / PORTABLE 1 \$9,788.92 (a) Totals 45 \$65,797.42</p> <p><u>CERTIFIED Inventory:</u></p> <p>TELEPHONE – OTHER EQUIPMENT –CELL / PORTABLE 1 \$9,788.92 (a)Texas Government Code, Annotated Section 403.273 (f)(g) requires each state agency to conduct an annual physical inventory of all personal property and certify the accountability of the inventory to the Comptroller on an annual (fiscal) basis. At all times, the property records of a state agency must accurately reflect the property possessed by the agency. The</p>	<p>I</p>	<p>Internal auditors obtained and reviewed inventory as of August 30, 2013 and determined that all 45 items have been deleted.</p> <p>No further work is deemed necessary in this area at this time.</p>

<p>Commission's property manual requires the Property Manager to adjust and update the inventory system at the end of the annual physical inventory for any discrepancies noted.</p> <p>Recommendation: The Commission should comply with Texas Government Code and follow the State Comptroller's State Property Accounting procedures to submit the proper documentation or forms to eliminate the 45 fixed asset items totaling \$65,797.42 in order for the Commission records to properly reflect the property inventory totals for the MOBILE and CERTIFIED inventories.</p> <p>Management's Response: <i>Management concurs with the finding and these records have already been deleted to reflect the trade in of the assets.</i></p>		
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I = Implemented

P = Partially Implemented

N = Not Implemented

Appendix 2:

ENTITY: Texas Alcoholic Beverage Commission

**PROJECT: Follow-up on prior Internal Audit Recommendations – (1) Tax Administration-Ports of Entry
(Report Date: March 07, 2013)**

FISCAL YEAR: 2013

PRIOR FINDINGS/RECOMMENDATIONS (issued by the Internal Auditor)	CURRENT STATUS*	Brief Description of Corrective Action Taken*
<p><u>Tax Administration-Ports of Entry</u></p> <p><u>Finding #1</u></p> <p>Finding 1: An established Destruction Schedule is not being followed by the ports of entry for the destruction of confiscated and abandoned merchandise as required by the POE policies and procedures manual. Currently the Agent destroying confiscated/abandoned items must be a commissioned officer. There is one commissioned Agent assigned in Region 3 who travels to all ports of entry to pick up the confiscated and abandoned items which need to be destroyed. During our visit to the Laredo ports of entry, we observed that confiscated/abandoned items were locked up in storage until the TABC Agent makes a trip to Laredo to pick up the items to be properly destroyed. There is no documented schedule for the destruction of the confiscated/abandoned items. Physical observation of the Laredo ports of entry building used to store the confiscated/abandoned items disclosed that the building is no larger than 10 feet by 12 feet in size and that a lack of storage space is starting to become an issue. Additionally, the same building is used for daily administrative functions such as keeping the TCOs cash box lockers, overnight deposit safe, personnel files, to perform daily cashbox and stamp reconciliations, and hold supervisory meetings with staff.</p> <p>Recommendation: The Ports of Entry Headquarters management should reconsider developing a Destruction Schedule for confiscated/abandoned items based on factors which would allow for the destruction of the majority of items throughout the 28 ports of entry. Some examples of factors for consideration are:</p> <ol style="list-style-type: none"> a. Volume of confiscated/abandoned items at each port of entry each year b. POE staffing at each port of entry: Full time/Temporary (seasonal traffic) c. Number of commissioned Agents assigned d. Geographical location and distance of each 	<p style="text-align: center;">I</p>	<p>Internal auditors obtained a sample of Destruction of Schedules for each Region and traced to supporting documentation showing that each schedule was followed.</p> <p>No further work is deemed necessary in this area at this time.</p>

- port of entry
- e. Security and safeguards of designated storage areas for abandoned/confiscated items

Additionally, the Commission management should monitor the space at each port of entry to ensure continued effectiveness of operations.

Management Response

Management concurs that Form P-934, Ports of Entry Confiscation Receipt, instructions notate “Confiscated items shall be secured and submitted to the Port Supervisor and the established destruction schedule shall be followed”. Further, that a destruction schedule had not been formally developed and implemented. Management is working on revising form P-934 as well as addressing the development and implementation of a schedule to destroy the retained alcoholic beverages.

Finding #2

Finding 2: Taxpayer Compliance Officer (TCO) weekend cash box audits are not being conducted at least once a month as required by the POE Policy, Procedures manual.

Each TCO at the ports of entry is assigned his/her cash box to use while on duty. The POE Policies and Procedures manual requires the port of entry Supervisors and Assistant Supervisors to conduct three (3) TCO cash box audits each month with one (1) of the three cash box audits being conducted on a weekend during the month. During the twelve (12) month period audited (2/1/2012 – 1/31/2013) only 68 (31.50%) weekend TCO cash box audits were conducted by the Supervisor and Assistant Supervisor from a projected 216 TCO weekend cash box audits. Also for the same 12 month period audited the port of entry Supervisor and Assistant Supervisor conducted a total of 663 TCO cash box audits resulting in 152 overages and shortages totaling a net minus (\$14.10).

Recommendation:

Ports of Entry – Headquarters management should re-evaluate the POE Policies and Procedures regarding the monthly number and specific days of TCO cash box audits required at the ports of entry. POE Headquarters management should take into

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Internal auditors determined that Ports of Entry management completed an update of the Policies and Procedures related to “TCO Audits” but they are waiting approval by the Policy Review Committee prior to the implementation of the changes. We encourage management to continue its efforts to ensure full implementation of our recommendation.

No further work is deemed necessary in this area at this time.

consideration the TCO revenue collection process controls in place, revenue and stamps reconciliation, reporting controls in the Port of Entry Tax Collection System (POETCS), potential revenue risks, and compare to the feasibility of personnel time and compliance costs involved in the current POE manual requirements.

Management’s Response:

Management Concurs with the findings and is in the process of re-evaluating and re-writing the policy and procedure regarding TCO cash box audits, taking into consideration risk based factors in determining the monthly number of audits per TCO and the number of weekday and weekend audits required. Updated policy and procedure should be tested and fully implemented by 08/31/2013.

Matters For Future Consideration

Revenue collections reported by the Commission for the Laredo ports of entry during fiscal year 2012 totaled \$1,273,536 with expenditures totaling \$676,461. The Laredo ports of entry accounted for approximately 23.4% of total revenue (\$5,433,118) collected by the 28 ports of entry in fiscal year 2012.

The Laredo ports of entry monthly average revenue deposits for December 2012 and January 2013 were \$210,135 and for the other 10 months of the year the monthly average was \$85,327.

Also during the 31 days from December 16, 2012 through January 15, 2013 reported revenue collections totaled \$314,474 (24.6% of Laredo’s FY 2012 annual revenue) with several daily deposits ranging from \$20,482 to \$25,789 in January 2013. All of this revenue activity occurred during regular working hours with the Laredo ports of entry closing at 12:00 am (midnight) each day.

During the months of December and January holiday season, traffic is heavy and constantly crossing the ports of entry at all hours due to all the festivities during that period. Management should research the possibility of extending the Laredo ports of entry hours opened for a certain period(s) of time during the months of January and December. Potential results include:

1. More effective compliance with the Texas Alcoholic Beverage Code and Cigarette Tax Code
2. Mitigation of potential loss of revenue over a short period of time with temporary costs paid with additional revenue collected.

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Internal auditors determined that a staffing analysis was conducted and necessary changes made as a result of our recommendation. One of the changes was extending the hours at specific ports, especially Laredo. We obtained and reviewed the extended hour schedule and records for the Laredo port from October 15, 2013 through June 2014 and noted no exceptions. We commend management for considering the internal auditors’ recommendation related hours of operation. The fiscal outcome of this recommendation will be considered as a part of future internal audit risk assessment.

No further work is deemed necessary in this area at this time.

<p>We also recommend that the Commission management conduct a pilot study by evaluating the hours of operation at other ports of entry.</p> <p>Management's Response: <i>Management is open to scheduling and staffing the ports at locations and times that will maximize tax collection for the State of Texas. As long as there is sufficient staffing to accommodate an extended late shift, and taking into consideration the safety climate of the individual ports, management may consider extending the port operation hours during the busy holiday season, particularly in the Laredo Port.</i></p>		
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Appendix 3:

ENTITY: Texas Alcoholic Beverage Commission

PROJECT: Follow-up on prior Internal Audit Recommendations – (1) Inspection Administration - Compliance (Report Date: June 05, 2013)

FISCAL YEAR: 2014

PRIOR FINDINGS/RECOMMENDATIONS (issued by the Internal Auditor)	CURRENT STATUS*	Brief Description of Corrective Action Taken*
<p><u>Inspection Administration</u></p> <p><u>Finding #1</u></p> <p>There is no procedure or instruction on how inspection time will be computed for completed inspections with different inspection times being recorded in the Agency Reporting and Tracking System.</p> <p>Three of ten (10) Form C-706 (Open Compliance Check Inspection) inspections tested had inspection times calculated differently: 1 inspection - using percentage of an hour 1 inspection - using minutes and 1 inspection - possible reporting error.</p> <p>Inspection Time Inspection ID per Form C-706 per ARTS 1650721 .75 45 minutes (percentage of hour) 1684218 .20 20 minutes (minutes) 1650922 .50 90 minutes (possible error)</p> <p>Recommendation: Management should include a procedure/comment on the method required to record inspection time at the completion of an inspection and ensure that the inspection time numbers on the inspection forms agree to the recorded Agency Reporting and Tracking System inspection time. It is essential that accurate inspection times be consistently recorded by field auditors since the number of hours worked by auditors are used by management in monitoring the inspection target numbers in the Commission’s annual Compliance Action Plan.</p> <p>Management’s Response <i>TABC Management concurs with the findings. Management will review inspections procedures related to this matter and develop a process to more efficiently account/record actual inspection times and ensure data entry is accurately reflected in the Agency Reporting and Tracking System. Projected Implementation: 6 Months</i></p>	<p style="text-align: center;">I</p>	<p>A new procedures manual related to inspections was implemented April 2014. The internal auditors obtained an excerpt of the manual and determined that it addressed our recommendations. Additionally, internal auditors obtained and reviewed evidence of the training class on the new procedures.</p> <p>No further work is deemed necessary in this area at this time.</p>

<p><u>Finding #2</u> Management should clarify policy on recording inspection time at the completion of an inspection.</p> <p>The five inspections reviewed at District 5 (San Antonio) had a range from 1 to 6 days from the date of the inspection to the date it was recorded in the Agency Reporting and Tracking System. The Compliance Procedures Manual requires that they be recorded “upon completion of an inspection”.</p> <table border="1"> <thead> <tr> <th>Inspection ID:</th> <th>Date of Inspection</th> <th>Recorded in ARTS /DAR</th> <th>Number of Days</th> </tr> </thead> <tbody> <tr> <td>1639351</td> <td>10/18/2012</td> <td>10/22/2012</td> <td>4</td> </tr> <tr> <td>1650721</td> <td>11/08/2012</td> <td>11/09/2012</td> <td>1</td> </tr> <tr> <td>1684218</td> <td>01/11/2013</td> <td>01/17/2013</td> <td>6</td> </tr> <tr> <td>1685565</td> <td>01/18//2013</td> <td>01/22/2013</td> <td>4</td> </tr> <tr> <td>1693234</td> <td>02/01/2013</td> <td>02/04/2013</td> <td>3</td> </tr> </tbody> </table> <p>Recommendation: Management should clarify the Compliance Procedures Manual to be more consistent as to when completed inspections are required to be recorded by field auditors in the Agency Reporting and Tracking System depending on the type of inspection. This would also establish reporting consistency in the five statewide districts and provide a more up to date number of inspections completed.</p> <p>Management’s Response: <i>TABC Management concurs with the finding. Management will review and amend the Compliance Procedure Manual to require that all inspections are recorded and data entered upon completion within a reasonable time to be determined by Management. Projected implementation: 6 Months.</i></p>	Inspection ID:	Date of Inspection	Recorded in ARTS /DAR	Number of Days	1639351	10/18/2012	10/22/2012	4	1650721	11/08/2012	11/09/2012	1	1684218	01/11/2013	01/17/2013	6	1685565	01/18//2013	01/22/2013	4	1693234	02/01/2013	02/04/2013	3	<p>I</p>	<p>A new procedures manual related to inspections was implemented April 2014. The internal auditors obtained an excerpt of the manual and determined that it addressed our recommendations. Additionally, internal auditors obtained and reviewed evidence of the training class on the new procedures.</p> <p>No further work is deemed necessary in this area at this time.</p>
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1693234	02/01/2013	02/04/2013	3																							

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Appendix 4

Objective, Scope, and Background Information

Objective

The objective of these internal audit follow-ups was limited to following up on the findings and recommendations included in the following:

- Fixed Asset Management (Report Date: January 31, 2013)
- Tax Administration – Ports of Entry (Original Report Date: March 07, 2013)
- Inspection Administration - Compliance (Report Date: June 05, 2013)

Scope

Our procedures included reviewing the previous audit reports, inquiring about the status of the reports' recommendation(s), discussions with Commission management, obtaining supporting documentation, and verifying the information.

Methodology

The Texas Alcoholic Beverage Commission management from the respective audit follow-up areas completed the *Prior Internal Audit Recommendation Schedules* to determine the current status of the prior audit findings, recommendations, and corrective actions taken by management for the Fixed Asset Management, Tax Administration – Ports of Entry, and Inspection.

Information collected and reviewed included the following:

- Original Audit Reports for:
 - Internal Audit of Fixed Asset Management (Original Report Dated: January 31, 2013)
 - Internal Audit of the Tax Administration – Ports of Entry (Original Report Dated: March 07, 2013)
 - Internal Audit of the Inspection Administration (Original Report Dated: June 05, 2013)
- Review of other pertinent reports and documents

Procedures and tests conducted included the following:

- Inquired about corrective actions taken by management for each report.
- Reviewed corrective actions taken by management for each report.
- Discussed the original report findings and the current status with the applicable division head.

- Reviewed recent State Auditor’s audit reports issued to determine if any of their audit results would affect or change our internal audit follow-up reports’ recommendations.
- Reviewed the Commission’s website to determine if there were changes that could impact the any of the audit areas being followed-up on.

Other Information

Our internal audit was conducted 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 internal audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our internal audit objectives. Our internal audit also conforms with the Institute of Internal Auditor’s (IIA) *International Standards for the Professional Practice of Internal Auditing*.

Appendix 5:

Background Information

In 1935, the Legislature created the Texas Alcoholic Beverage Commission (formerly the Texas Liquor Control Board).

The Texas Alcoholic Beverage Commission (TABC) is the state agency that regulates all phases of the alcoholic beverage industry in Texas. The duties of the Commission include regulating sales, taxation, importation, manufacturing, transporting, and advertising of alcoholic beverages.

The TABC collects in excess of \$200 million annually in taxes and fees, which aids in the financing of the state's public schools, local governments, research, human services, and other areas in which state government provides services to all Texans.

The Alcoholic Beverage Code, which was enacted to protect against involvement of the criminal element in alcoholic beverage trafficking authorizes the Texas Alcoholic Beverage Commission to:

- Grant, refuse, suspend, or cancel permits and licenses in all phases of the alcoholic beverage industry;
- Supervise, inspect, and regulate the manufacturing, importation, exportation, transportation, sale, storage, distribution, and possession of alcoholic beverages;
- Assess and collect fees and taxes;
- Investigate for violations of the Alcoholic Beverage Code and assist in the prosecution of violators;
- Seize illicit beverages;
- Adopt standards of quality and approve labels and size of containers for all alcoholic beverages sold in Texas;
- Pass rules to assist the agency in all of the above.

The Governor, with the advice and consent of the Senate, appoints three public members of the Commission for staggered six-year terms.

The Commissioners appoint an Executive Director who supervises the Commission's activities. The Commission's operating budget is prepared and approved by the Commission on an annual basis, whereas the State legislative appropriation request is determined every two years. Both the budget and appropriations are reviewed and approved by the State Legislature.

The Commission is divided into thirteen divisions: Executive; Field Operations – Enforcement, Audit & Investigations, Ports of Entry; Business Services; Education and Prevention; Human Resources; Information Resources; Legal Services/General Counsel; Licensing; Office of Professional Responsibility; Tax and Marketing; and Training. The Executive Division, which is headed by the Executive Director, provides oversight of the Deputy Executive Director, Director of the Office of Professional Responsibility, and the Director of Communications and Government Relations. The other divisions report directly to the Deputy Executive Director while General Counsel reports directly to the Commissioners.

The Commission generates revenue from alcoholic beverage license and permit fees, alcohol beverages taxes, cigarette taxes, airline beverage tax, and revenue collected on audits. This revenue is deposited into the General Revenue Fund.

Appendix 6:

Report Distribution

As required by Gov't Code 2102.0091, copies of this report should be filed with the following:

Governor's Office of Budget, Planning and Policy

Attn: Kate McGrath
internalaudits@governor.state.tx.us

Legislative Budget Board

Attn: Ed Osner
Ed.Osner@lbb.state.tx.us

State Auditor's Office

Attn: Internal Audit Coordinator
iacoordinator@sao.state.tx.us

Sunset Advisory Commission

Attn: Ken Levine
sunset@sunset.state.tx.us

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Steven M. Weinberg, MD, JD
Ida Louise "Weisie" Steen

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Sherry Cook, Executive Director