

DEPARTMENT OF ALCOHOLIC BEVERAGE CONTROL

**REPORT ON AUDIT
FOR THE YEAR ENDED
JUNE 30, 2012**



AUDIT SUMMARY

We have audited the basic financial statements of the Department of Alcoholic Beverage Control as of and for the year ended June 30, 2012 and issued our report thereon, dated September 28, 2012. Our report is included in the Department's Annual Report, is available at the Auditor of Public Accounts' website at www.apa.virginia.gov and at the Department of Alcoholic Beverage Control's website at www.abc.virginia.gov.

Our audit of the Department of Alcoholic Beverage Control for the year ended June 30, 2012, found:

- the financial statements are presented fairly, in all material respects;
- internal control findings requiring management's attention; however, we do not consider them to be material weaknesses; and
- no instances of noncompliance or other matters required to be reported under Government Auditing Standards.

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INTERNAL CONTROL FINDINGS AND RECOMMENDATIONS

Improve Controls over the MIPS to Performance Interface

The Department of Alcoholic Beverage Control's (ABC) staff is not regularly reviewing Management of Inventory and Product Sales (MIPS) data, which can lead to adjustments that affect prior periods and can result in misstatements and losses. While ABC's MIPS system does not properly interface with the Performance Financial System, staff prepares monthly adjustments to bring the financial system in balance with MIPS from real time reports and to reconcile MIPS to Performance at year end. Therefore, any MIPS adjustments prepared after the report run date are not in the Performance system.

Staff periodically review and correct MIPS data; however there is no regular schedule or routine for processing the correction or conducting the review. For example, the Total Dollar Value of Inventory Report as of June 30, 2012 prepared on July 16, 2012 did not equal the same report prepared on September 7, 2012. A discrepancy between these reports arose from corrections entered into MIPS with no corresponding entry in Performance at year end.

ABC should require monthly reviews and the correction of any discrepancies after properly investigating the differences in the MIPS System. MIPS data should be accurate when the financial team brings Performance in balance in order to have properly represented financial statements.

Update IT Risk Management and Contingency Plans

ABC has not updated its Information Technology (IT) risk assessments or its disaster recovery contingency plans for its software applications that contain confidential and mission critical data since 2007. By not updating the risk assessments or disaster recovery contingency plan, ABC incurs a significant risk because the agency's systems have substantially changed since ABC originally created the plans. Without updated risk assessments and disaster recovery plans for its applications, ABC cannot accurately determine the appropriate information security safeguards to protect data or develop adequate plans to recover from a disaster or major system failure. This would result in unnecessary and potentially material financial losses from system unavailability and data confidentiality problems. In addition, the Commonwealth's Information Security Standard, SEC 501-06, requires agencies to maintain updated IT risk management and contingency plans for all sensitive applications and systems.

Updated plans are especially important during times of transition and change. As ABC and the IT Partnership with Northrop Grumman begin the process to plan moving the servers from ABC's headquarters to the Commonwealth's enterprise data center, the ability to reference updated recovery plans is very important. ABC will need to update these plans again once it has completed the move. ABC should consider establishing written restoration processes for its applications for use until the server move is complete.

We recommend that ABC develop current disaster recovery procedures for its applications that ABC can use until IT Partnership fully transitions the servers to the enterprise data center. Once fully transitioned, we recommend that ABC updates its risk assessments and contingency plans to reflect the final environment.



Commonwealth of Virginia

Auditor of Public Accounts

Walter J. Kucharski
Auditor of Public Accounts

P.O. Box 1295
Richmond, Virginia 23218

September 28, 2012

The Honorable Robert F. McDonnell
Governor of Virginia

The Honorable John M. O'Bannon, III
Chairman, Joint Legislative Audit
And Review Commission

Alcoholic Beverage Control Board
Department of Alcoholic Beverage Control

INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS

We have audited the basic financial statements of the **Department of Alcoholic Beverage Control** (ABC) as of and for the year ended June 30, 2012, and have issued our report thereon dated September 28, 2012. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

Management of the ABC is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered the ABC's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the ABC's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the ABC's internal control over financial reporting.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above. However, we identified certain deficiencies in internal control over financial reporting entitled "Improve Controls over the MIPS to Performance Interface" and "Update IT Risk Management and Contingency Plans," which are described in the section titled "Internal Control Findings and

Recommendations,” that we consider to be significant deficiencies in internal control over financial reporting. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the ABC’s financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under Government Auditing Standards.

The ABC’s response to the findings identified in our audit is included in the section titled “Agency Response.” We did not audit the ABC’s response and, accordingly, we express no opinion on it.

Status of Prior Findings

The ABC has taken adequate corrective action with respect to audit findings reported in the prior year.

Report Distribution and Exit Conference

The “Independent Auditor’s Report on Internal Control over Financial Reporting and on Compliance and Other Matters” is intended solely for the information and use of the Governor and General Assembly of Virginia, the Alcoholic Beverage Control Board, and management, and is not intended to be and should not be used by anyone, other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

We discussed this report with management at an exit conference held on November 2, 2012.

AUDITOR OF PUBLIC ACCOUNTS

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COMMONWEALTH of VIRGINIA

Department of Alcoholic Beverage Control

COMMISSIONERS

J. NEAL INSLEY, CHAIRMAN
SANDRA C. CANADA
BRYAN M. RHODE

CHIEF OPERATING OFFICER/ SECRETARY TO THE BOARD
W. CURTIS COLEBURN, III

October 26, 2012

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Mr. Walter J. Kucharski
Auditor of Public Accounts
James Monroe Building
101 North 14th Street
Richmond, VA 23219

Dear Mr. Kucharski:

The Virginia Department of Alcoholic Beverage Control appreciates the opportunity to comment on the Auditor of Public Accounts most recent audit report for ABC. This letter provides ABC's response to the internal control findings and recommendations noted during the audit of our 2012 financial statements. ABC strives to maintain an effective system of internal controls over financial reporting and operations and is pleased that the report contains no significant or financial-related findings. The report did contain two recommendations: 1) Improve Controls Over the MIPS to Performance Interface, and 2) Update IT Risk Management and Contingency Plans. ABC concurs with both findings. Listed below are the Department's responses to the recommendations.

Improve Controls over the MIPS to Performance Interface

ABC concurs that there is no regular routine for reviewing and correcting MIPS data. We are currently working on developing several processes that will provide for both automated and manual review of MIPS, and these are detailed below.

The difference of \$1,435 in the "Total Dollar Inventory Value On Hand" amounts on the reports prepared on July 16 and September 7 were due to the corrections discussed below. The report is a "real time" report and will reflect the total balance on hand as of a specific date. Because the corrections made were for prior periods, the inventory amounts changed to reflect the corrections as of those dates. If the report had been a historical report, the amounts would not have changed.

The specific corrections entered into MIPS to which the APA are referring occurred at the end of August, 2012, and therefore will be reflected in Performance during the next monthly reconciliation, in September. The corrections that were made were due to stale "in transit" inventory items that had not been cleared out of the system when stores received in special orders with their regular shipments. The corrections dated back to 2010 and totaled \$1,435 out of a total inventory balance on hand of \$84,158,402. ABC realizes that the corrections related to prior periods, however, the amount was immaterial (.0017%) to our financial statements and therefore no restatement was necessary. This amount will be adjusted in Performance during the next reconciliation and the 2 systems will be in balance. As the systems are reconciled each month, ABC does not concur that adjustments are not properly posted in Performance or that the adjustments can result in misstatements or losses.

Mr. Walter J. Kucharski

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ABC will develop a mechanism for retaining the historical monthly inventory values. ABC ITSD is currently working on developing an historical report for use by Finance and auditors, and will modify the report descriptions to differentiate between the real time report and the historical data report. This report should be complete January 30, 2013.

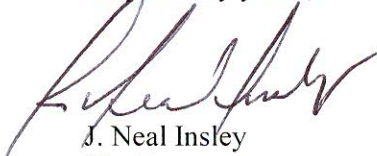
Since the corrections made were the result of last minute special orders remaining in transit and not being closed, ABC will develop a calendar picker for all ordering that will enforce delivery dates in alignment with actual store delivery dates. This will reduce the frequency of stale orders and the need for corrections. ABC ITSD will also develop a MIPS job to automatically close stale orders where possible and provide an email notice to the stores to prompt resolution of any outstanding in transit items. These items should be complete by January 30, 2013. And to further ensure financial statement accuracy, ABC personnel will perform an annual review of the MIPS data in June of each year, prior to year end closing. This will be a written procedure and will be in place for June, 2013.

Update IT Risk Management and Contingency Plans

ABC concurs that Risk Management and Disaster Recovery are required and important parts of the Information Security Program. ABC has implemented a Risk Management strategy to complete the process, and has engaged additional resources to begin documenting the disaster recovery process.

ABC would like to restate again its commitment to an effective system of internal controls and an effective information security program. We have and will continue to make this a priority and allocate the necessary resources to ensure the continued protection of the Commonwealth's data. As always, we appreciate the diligence and professionalism of your staff along with the opportunity to respond.

Respectively yours,



J. Neal Insley
Chairman

DEPARTMENT OF ALCOHOLIC BEVERAGE CONTROL BOARD MEMBERS

As of June 30, 2012

J. Neal Insley
Chairman

Sandra C. Canada

Bryan M. Rhode