

Virginia ABC

Overview of Operations and Budget

House Appropriations Public Safety Subcommittee
January 10, 2019

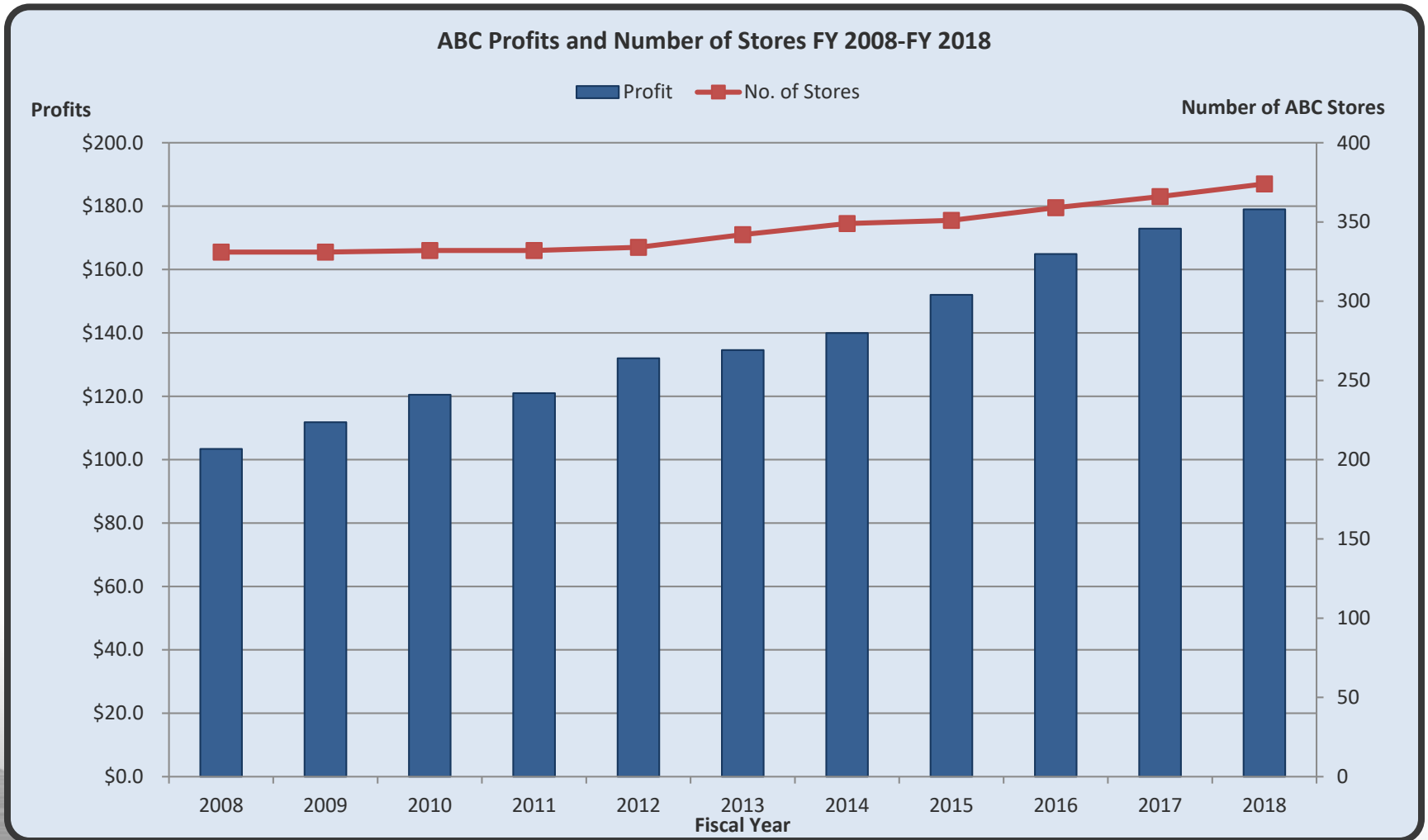
Travis G. Hill, CEO Virginia ABC



Current State of the Control State

- **Mission Critical Statistics**
 - FY 2018 Gross Sales of \$983 million (up 4.2%)
 - FY 2018 Profits of \$181 million (up 4.6%)
 - Retail Licenses: 19,190 (up 1.3%)
 - Total Cases shipped to ABC stores: 5,070,262 (up 4.2%)
 - ABC store underage sales compliance – 99%
 - Licensee underage sales compliance – 90%
- **Operating Expense**
 - FY 2018: \$665.4 million
 - FY 2018 Operating expenses include: alcohol – 71.1%, personnel - 17.1%, retail occupancy - 4.8% and contractual (VITA, freight) - 5.2%
- **Employee Numbers**
 - ABC currently has over 4,000 total employees
 - 1,190 full-time employees
 - 2,836 part-time employees

Historical Sales Growth



Licensing and Enforcement

- Bureau of Law Enforcement
 - 110 employees
 - 88 sworn agents in 9 field offices
 - Field agents focus on retail and banquet license investigations
 - Compliance agents handle wholesale and manufacturer licenses
 - 22 civilian staff in Licensing and Records Management
 - Almost 19,000 retail licensees
 - 24,000 one-day banquet licenses
 - Activities include site inspections, application investigations, covert observations, planned operations and criminal investigations
 - Tax Management responsible for \$80M in excise tax collections
- Hearings Division
 - Adjudicates almost 500 cases annually
 - Most frequent cases involved underage sales and mixed beverage ratio (§4.1-114)

Enforcement Activities

- Direct Shipping continues to be a focus for enforcement.
 - Unlicensed Shippers- Virginia ABC has identified in excess of 650 Unlicensed Shippers and has developed and implemented a plan to seek compliance and proper licensing of these unlicensed shippers.
 - Virginia ABC is partnering with the Virginia licensed common carriers to stop the unlicensed shippers from shipping into Virginia.
 - This activity is responsible for loss of revenue to Virginia through excise taxes and sales taxes not being collected.
- During 2019 Virginia ABC will work with stakeholders on License Reform and Modernization.
 - Review will include all manufacturing, wholesale, and retail licenses. Goal is to look for ways of consolidation and simplification of current structure.
 - All fees will also be reviewed.

Contributions to Commonwealth Last 7 Years Total \$2.9B

FY 2018 increased \$19 million over FY 2017, \$108m over FY 2012

Dollars in Millions

Revenue Source	FY 2012	FY 2013	FY 2014	FY 2015	FY 2016	FY 2017	FY 2018
ABC profit transfers	\$132.0	\$134.6	\$140.0	\$152.0	\$164.9	\$171.2	\$180.8
State taxes	\$121.0	\$126.8	\$132.0	\$139.8	\$147.8	\$154.4	\$161.5
General sales tax	\$29.6	\$31.3	\$36.9	\$39.2	\$41.3	\$43.3	\$45.4
Wine liter tax	\$33.5	\$34.4	\$34.6	\$35.2	\$36.2	\$36.8	\$38.2
Malt beverage tax	\$43.7	\$42.8	\$43.3	\$42.9	\$43.2	\$42.8	\$42.9
Total	\$359.7	\$369.9	\$386.9	\$409.3	\$433.4	\$448.6	\$467.2

Profit Forecast

Financial Forecast – Revenue (Sales)

**Sales Forecast – 4.85% increase in FY2019;
4.6% increase FY2020**

- Industry growth rates projected at 4.0% for FY2018 – 2021
- The forecast includes adjustments for changes in the number of Friday and Saturday sales vs. Sunday through Thursday sales (calendar impacts)
- FY2019 extended Sunday hours at select ABC stores
- Timing of holidays – 2018 longest possible holiday season, 2019 the shortest
- FY 2018 actual sales within 0.1% of forecast

Appropriation Act Profit Requirement

	<u>FY 18</u>	<u>FY 19</u>	<u>FY 20</u>
Profit Transfer Required by Code	104,100,000	109,800,000	115,500,000
Dept of Behavioral Health and Developmental Services	65,375,769	65,375,769	65,375,769
Other State Agencies	187,906	187,925	187,925
Operating Efficiencies	3,864,585	3,864,585	3,864,585
Deferred VRS	500,882	1,001,765	-
2018 Approp Act Required Profit Transfer	174,029,142	180,230,044	184,928,279
HB1700 Adjusted Forecast Profit Transfer	180,800,000	182,800,000	186,700,000

Financial Forecast – P & L

GACRE FY 2019 – FY 2024

(\$ million)

	FY2018	FY2019	FY2020	FY2021	FY2022	FY2023	FY2024
Revenue Sources:							
		4.85%	4.60%	4.25%	4.25%	4.25%	4.25%
Alcoholic Beverages (Store Sales)	983.3	1,031.0	1,078.4	1,124.3	1,172.0	1,221.9	1,273.8
Less: State Taxes on Spirits & Wine	161.0	169.9	177.7	185.3	193.1	201.3	209.9
Net Store Sales	822.3	861.1	900.7	939.0	978.9	1,020.5	1,063.9
Other Revenue	22.3	23.1	23.3	23.6	23.8	24.0	24.3
Total ABC Revenue	844.6	884.2	924.1	962.6	1,002.7	1,044.5	1,088.2
Cost of Goods Sold:	473.7	496.5	519.3	541.3	564.3	588.8	613.8
Operating Costs:	191.7	205.0	218.1	226.4	234.3	243.9	255.4
Infrastructure Projects:	-	-	-	4.9	11.2	15.5	18.4
GASB 87: Preliminary Estimate	-	-	-	2.1	1.2	0.6	-
ABC Net Profit	179.2	182.8	186.7	187.9	191.6	195.7	200.5

GASB – Standard No. 87

Governmental Accounting Standards Board

- Effective for the Commonwealth and ABC on July 1, 2020 (Fiscal Year 2021)
- Provides a single model for lease accounting across all government entities
- Assumes all leases are **financing** the right to use an asset
- Significantly changes the accounting methodology for leases

Financial Impact of GASB 87

Single Store Illustration

Gainesville, VA

- Opened 3/1/2009
- 5 year lease with 5 year option to renew
- Assume renewal option will be exercised
- Interest rate has significant P&L impact

	Current	3.5%	S/L	Total Expenses after	P & L Impact After
	<u>Rent</u>	<u>Interest</u>	<u>Amortization</u>	<u>GASB 87</u>	<u>GASB 87</u>
FY 2017	\$ 93,509				
FY 2018	\$ 95,379				
FY 2019	\$ 97,286				
FY 2020	\$ 99,232				
FY 2021	\$ 101,217	\$ 11,386	\$ 97,183	\$ 108,569	\$ 7,352
FY 2022	\$ 103,241	\$ 8,158	\$ 97,183	\$ 105,341	\$ 2,100
FY 2023	\$ 105,306	\$ 4,743	\$ 97,183	\$ 101,926	\$ (3,380)
FY 2024	\$ 80,157	\$ 1,198	\$ 72,887	\$ 74,085	\$ (6,072)
	\$ 775,327	\$ 25,485	\$ 364,436	\$ 389,921	\$ -

GASB 87 Impact on ABC

- Financial Management Impact
 - ABC has numerous capital leases, both retail space and equipment
 - ABC Profit will be negatively impacted during first 2 to 3 years of implementation
 - Lease Accountant Position created
 - New Financial System
 - GASB 87 Compliance was a key requirement for the new system.
 - Lease administration becomes an accounting function
 - Must have strong knowledge of Accounting to process the monthly rent payments and other costs such as CAM charges (which are tracked by lease).

Operating Budget Items

Biennium Amended Budget Proposals

All NGF funds are represented in \$000

Request	FY2019	FY2020	Description
Positions and Funding for New Store Openings – 9 positions	\$964.9	\$2,608	Opening an additional 9 stores during FY 2019.
Additional Civilian Administrative/Licensing Technicians – 7 positions	\$0	\$0	Funding approved in FY 19 Budget but MEL was not increased.

HB1770 (Knight)

Sunday Hours/Distillery Store Commission

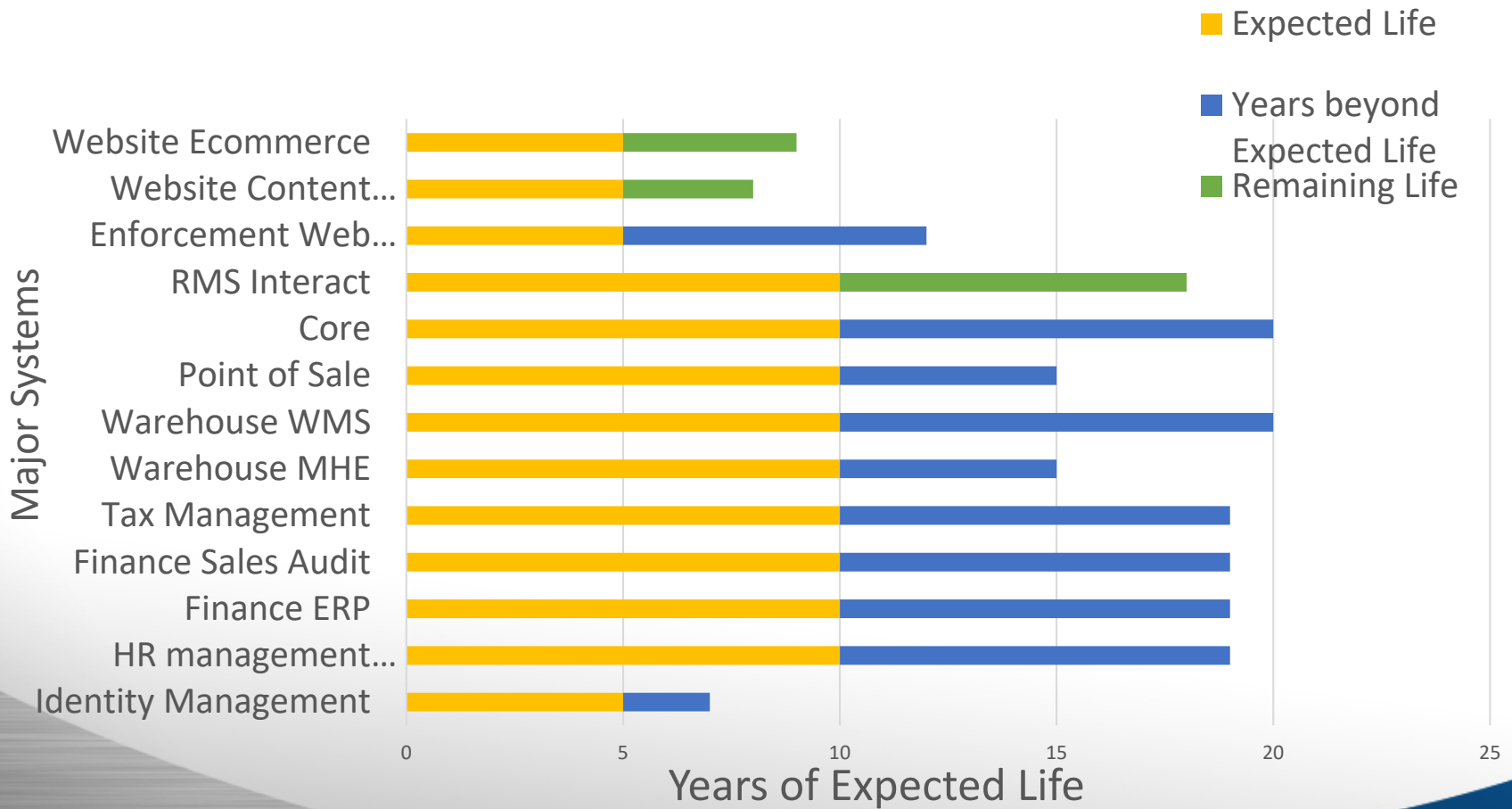
- Additional hours, 10 am to noon, generate sales equal to 25% of the current average Sunday hourly volume.
- \$13,520 in additional sales per store open per year
- \$3,245 in additional profit per store open per year
- Distillery store sales continue to grow approximately 30% per year to \$6.5M in FY 2020
- Increasing commission from 8% to 20% on forecast FY 2020 distillery sales increases commission expense by \$784,112
- Approximately 240 stores open an additional 2 hours generates sufficient additional profit to cover the added commission expense

IT Reinvestment Program

ABC IT Modernization

- Assessment conducted as part of a 2014 review of ABC's Operations determined aging IT infrastructure threatened operations and revenue generation
 - Virginia ABC operating outdated systems that are either out of support or soon to be out of support
 - Several more major systems, while now compliant, will become deficient – Finance, Point of Sale, Sales Audit, Inventory Management, and HR
- Modernization plan presented to Administration and General Assembly in 2015
 - Remediate aging systems and allow for continued growth
 - ABC estimated \$65 million needed over six years for technology upgrades
 - Figure includes the \$25 million for projects approved in 2015
- ABC is also progressing in closing existing VITA security exceptions and APA audit points
 - Remaining open points result of deficiencies in antiquated IT systems
 - Projects underway will address additional security exceptions

Expected Life of ABC Systems Compared to Current System State



Projects Included in Chapter 665 of the 2015 Appropriation Act

Item	Status
Financial Management System	Go Live on schedule for 7/1/19
Licensing System	Go Live on schedule for Q1 2020
Website Phase II	Complete
Broadband for Stores	Complete
Electrical System	Deferred

Financial System Replacement

- Oracle Fusion Cloud Selected
- Contract Signed / project Commenced July 2018
- Accenture selected as Systems Integrator / Implementation partner
- Design and deploy workshops commenced
- First system fully independent of VITA – will use ABC Identity management (not COV) for user access controls
- Little customization (reports, interfaces, Business Intelligence)
- Standard Package includes Disaster Recovery, technical infrastructure and support
- Project Timeline
 - Commenced July 2018
 - Design through September 2018
 - Budgeting goes live first (approximately March 2019)
 - Core finance goes live for FY 2020 on July 1 2019
 - 3 month 'Hypercare' planned post go live

Licensing System

- Accela Civic Portal Selected
 - Commenced February 2018
 - Proceeding with phased approach of license categories
 - Banquet licenses first phase
 - Engaging with users to test modules as they are produced
- Project Timeline
 - Contract early 2018
 - Jan 2019 Accela Development completes
 - March – June ABC integration development completes
 - Integrated system testing, documentation and training July – January 2020
 - Go Live Q1 2020

Projects Included in Chapter 2 of the 2018 Appropriation Act

Item	Status
Point of Sale/Sales Audit	RFP Scoring
Email Migration	Completed 4/2018

Point of Sale/Sales Audit

- Entirety of ABC's Point of Sale and Sales Audit System end of life in two years
 - ABC must replace over 1,000 “lanes” of equipment and 400 store servers
- Extending current life not feasible
 - Higher costs incurred with extended life contracts
 - Higher failure rates
 - Shortage of equipment – delay or prevent store openings
 - Non-compliant with security standards – jeopardizes ability to take credit card payment (60% of sales)
- New system gives modern retailing opportunities
 - Multi-channel sales (ecommerce)
 - Real-time inventory
 - Customer programs – loyalty, coupons, mobile payment, etc.

Point of Sale/Sales Audit Pilot

- Biennium funding (\$15.4M) will acquire and pilot a new POS and Sales Audit System in up to five stores.
 - Covers license acquisition, hardware and software, implementation and maintenance
- Additional funding in the next biennium would be required to acquire and deploy the new systems across all ABC stores.
- The initial pilot will also provide more accurate costs for the deployment phase of the project.

Email / SharePoint Migration

- Office 365 Email migration & cutover is complete
Outlook successfully going live 4/16/18
 - 90% of mailboxes had no issues day one; @30 days < 2% of users were reporting an issue (20 users)
 - SharePoint migrated and upgraded to current version
 - Closed out execution phase within approved budget of \$1.2M

Email / SharePoint Migration

- Subsequent feature changes
 - Added desktop to desktop / consumer video capability using Skype and Teams (Hearings)
 - License True-Up completed decreased annual costs by \$30K with improved license mix (more lower cost users).
 - ABC is now responsible for SharePoint and hosted email governance
 - Commenced BYOD policy to reduce agency owned mobile devices
 - Deployed store portal in SharePoint to reduce dependency on email to stores
 - Created ABC's own Active Directory for ERP, EVA, Licensing and future new applications

Future ABC IT Projects

Item	Target Completion	Rationale
Website Phase III	2019	Driven by Web Strategy project from FY 2018
Identity Management	2019	Obsolete components – security exception required
Warehouse Management (MIPS)	Tied to Building Decision	Conveyor system and transportation system – needed in current or new facility – security exception required
Inventory Management	Tied to Building Decision	Same as above – Unable to support real time inventory
Tax Management	2020	Using outdated TAX software, many submissions manually keyed – security exception required
Human Resource/Payroll	2022	Homegrown system with limited functionality; requires software development for updates; needs update for Authority Transition– security exception required

FY 2019 Mid-Year Results

Store Growth

Store Count at 12/31/18 374

During FY 18 and to date FY 19

- Ten Stores Opened
 - Suffolk
 - Alexandria
 - Forest
 - Lebanon
 - Loudon – 2 locations
 - Fairfax – 2 locations
 - Stafford
 - Chesapeake
- Four stores Relocated
 - Portsmouth, Fairfax, Madison Heights, Leesburg
- Five stores Expanded
 - Powhatan, Marshall, Grafton, Garrisonville, Chesterfield
- Fourteen stores Updated

Holiday Campaign

- First ever statewide advertising supporting promotional offers throughout the holiday season (October 22-December 31) - utilizing Radio, Television, Digital and Social Media
- Goals
 - Premiumization – move consumers to a higher tier item
 - Expose consumers to luxury brands across categories
 - Utilize long holiday season of 2018
 - Increase overall sales
 - Increase bottles per transaction
 - Increase number of transactions
 - Increase average bottle price

Holiday Campaign

Door Busters

- Discounts over a three day period on specified 1.75L products; supported by manufacturer
- 802% increase in sales volume; 975% increase in bottle volume

Black Friday

- 20% discount on in-store purchases over \$100; supported by Virginia ABC
- 25% increase in sales volume; 20% increase in bottle volume over Black Friday 2017

Cyber Monday

- 20% discount on all purchases made on ABC eCommerce site; supported by Virginia ABC
- 113% increase in sales volume; 48% increase in order volume

Spirited Thursdays

- 20% discount on specified products; Focused on brands in a different category each week
- Rum – 1015% increase in sales volume; 1266% increase in bottle volume
- Cordials – 415% increase in sales volume; 530% increase in bottle volume
- Tequila – 830% increase in sales volume; 1041% increase in bottle volume
- American Whisk(e)y – 820% increase in sales volume; 926% increase in bottle volume
- Gin – 628% increase in sales volume; 660% increase in bottle volume
- Scotch – 1746% increase in sales volume; 2324% increase in bottle volume

FY 2019 Results to Date

Virginia ABC Authority
Sales and Profit as of 11/30/2018
(\$000)

	FY 2019 Actual	FY 2018 Actual	Growth	%
Gross Revenue	\$ 435,795	\$ 405,371	\$ 30,424	7.5%
Spirits Excise Tax	\$ 69,398	\$ 65,100	\$ 4,298	
Revenue from Operations	\$ 366,397	\$ 340,271	\$ 26,126	7.7%
Cost of Goods Sold	\$ 203,692	\$ 191,676	\$ 12,016	6.3%
Gross Profit	\$ 162,705	\$ 148,595	\$ 14,110	9.5%
Operating Costs	\$ 83,161	\$ 77,265	\$ 5,896	7.6%
Net Profit	\$ 79,544	\$ 71,330	\$ 8,214	11.5%

Profit Transfer Per 2018 Approp Act	\$179,730
Profit Transfer Per HB1700	\$182,800

FY 2019 Sales Results to Date through 12/29/2018

(\$000)

	Actual <u>FY 19</u>	Actual <u>FY 18</u>	Difference		Forecast <u>FY 19</u>	Difference	
			<u>\$</u>	<u>%</u>		<u>\$</u>	<u>%</u>
Sales	\$ 537,915	\$ 506,970	30,945	106%	\$528,141	\$ 9,774	101.9%

- Sales and profit through first 6 months of FY 19 are on track to achieve increased full year profit forecast