

STATE OF UTAH
OFFICE OF THE UTAH STATE AUDITOR



TINA M. CANNON
UTAH STATE AUDITOR

Department of Alcoholic Beverage Services

Agreed-Upon Procedures

For the year ended June 30, 2025

Report No. 25-01

Office of the Utah State Auditor

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TINA M. CANNON
UTAH STATE AUDITOR

Management Letter No. 25-01

April 24, 2025

Members of the Utah Alcoholic Beverage Services Commission

And

Ms. Tiffany Clason, Executive Director Department of Alcoholic Beverage Services

Commissioners and Ms. Clason:

Pursuant to *Utah Code 32B-2-302*, with the agreement of the Alcoholic Beverage Services Commission, and relating to the audit scope and focus described in the "State Auditor Proposed Audit Plan for Fiscal Year 2025", the Office of the Utah State Auditor has completed the annual audit of the Department of Alcoholic Beverage Services (DABS). In addition to our statutory audit responsibilities, the scope of this audit was expanded to investigate DABS concerns related to the potential theft of change order funds.

The procedures of this audit do not constitute an audit conducted in accordance with generally accepted auditing standards, the objectives of which would be the expression of an opinion on DABS's internal control. Accordingly, we do not express such an opinion.

This audit was conducted beginning February 2025 and included both financial and regulatory reviews. The financial scope of the audit included a review of DABS's accounting system, including how financial data is recorded and reconciled with the statewide accounting system. Additionally, the bank reconciliation process and cash handling procedures were evaluated. The regulatory scope of the audit provided an assessment of oversight and monitoring procedures for Type 5 Package Agencies, as well as a review of compliance with budgetary policies and procedures.

Audit Findings:

The audit identified nine separate findings, for which the full details and agency responses are included in the audit report. The findings can be summarized into three specific categories:

- **Cash Handling and Potential Theft:** We identified lapses in internal control procedures that contributed to the risk of theft. While these weaknesses allowed for the possibility of misappropriated funds, we also noted that DABS has since taken steps to strengthen its internal controls, particularly in early detection and response mechanisms.

- **Type 5 Package Agency (PA) Accounting and Oversight:** Oversight of Type 5 PAs remains an area of concern. In particular, DABS should take steps to implement more rigorous processes to track and account for funds remitted by these agencies to ensure completeness and accountability.
- **General Accounting System and Financial Reporting:** While DABS has made progress in addressing issues raised in prior audits, several areas remain unresolved. Continued improvements in system integrity and reporting accuracy are still necessary to meet best practices and ensure reliable financial management.

Audit Recommendations:

We encourage DABS to maintain the progress it has made thus far and to commit to both short-term and long-term improvements. Specifically, we recommend the following three managerial and oversight actions be taken immediately:

- Finalize and enforce updates to the DABS's cash handling policies to close existing control gaps.
- Strengthen oversight mechanisms for Type 5 Package Agencies, including improved tracking, reporting, and follow-up procedures related to the collection and remittance of funds.
- Continue efforts to modernize and reconcile the general accounting system, resolve the remaining discrepancies as detailed in the findings.

These measures will help safeguard public resources, ensure accurate financial reporting, and promote greater transparency and accountability.

We appreciate the cooperation of DABS management and staff throughout the audit process and are available to provide clarification or further guidance as the DABS implements these recommendations.

Sincerely,



Bertha Lui, CPA

Audit Director

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Background for Findings 1-3

In July 2024, DABS management requested the Office of the Utah State Auditor's (Office) assistance with reviewing a potential misappropriation of funds. While performing a bank reconciliation, a DABS employee discovered discrepancies related to the change orders at a State Liquor and Wine Store (Store) located in Salt Lake County. We commend DABS for detecting the discrepancies and reporting the situation to the Office.

Change orders occur when DABS stores request small bills and change from the bank to replace large bills in their tills. When the bank provides these small bills and change, it records a currency/coin shipment transaction (Shipment). DABS policy¹ requires the stores to return an equivalent amount in larger bills back to the bank (Deposit) within a short time-period, which the bank records as a standard cash deposit. These change orders occur routinely at most stores, typically once or twice a week. Because change orders are handled directly with the bank, they are performed outside of the DABS accounting system and thus no official DABS record is made of the transaction at the time of Shipment and Deposit.

On a regular basis, DABS stores deposit cash from liquor sales. The bank records these store revenue deposits separately from change order Deposits. When processing these store revenue deposits, the bank initially records the amount documented on the deposit slip and then verifies the cash at a later time. If the bank discovers a discrepancy during the cash verification process, it adjusts the depositor's account through either a currency short or a currency over transaction.

Findings & Recommendations 1-3

Finding 1. Missing Change Order Funds

We analyzed all change orders of the subject store for the period January 2021 to June 2024 and found that Deposits were \$112,809 less than the associated Shipments. We would not expect there to be any difference in amount between the change order Shipment and the subsequent Deposit since the DABS change order policy in effect at the time required that Shipments "be repaid immediately and in their entirety." Our analysis included the following procedures:

- We obtained the monthly bank statements, which document the Shipment and Deposit amounts, and determined that 136 of 235 (58%) Deposits contained less cash than the associated Shipment(s), resulting in the missing change order funds. We found that the

¹ DABS Policy Number 09-03

discrepancies for each shorted Deposit were initially in the \$200 to \$600 range, but over time progressed to \$1,000 to \$2,000, and were almost always round, even dollar amounts.

- We obtained armored car service logs and Store-prepared deposit slips, when available. We reviewed the preparer's initials on the logs and analyzed the handwriting on the deposit slips and determined that one individual handled the majority of the Shipments and Deposits.
- We interviewed certain current Store employees and based on their statements, verified that the same individual was primarily responsible for change order Shipments and Deposits.

Neither DABS management nor our Office were able to locate or account for the missing change order funds and it appears that the funds were likely misappropriated. These change order discrepancies continued without detection over an extended period of time because the DABS change order policy was inadequate, and bank reconciliations were not being properly performed.² We note that DABS was in the process of correcting their bank reconciliation process when the discrepancies were discovered and has since strengthened their change order policy. We reviewed DABS updated change order policy and noted further improvements can be made related to timing of deposits; see Finding 3 below.

Recommendations:

We recommend DABS:

- Implement the change order policy recommendation as described in Finding 3 below to ensure Deposits are made in a timely manner.
- Work with the Attorney General's Office to pursue additional criminal investigation.
- Consider seeking reimbursement from responsible individuals.

DABS' Response:

The Department of Alcoholic Beverage Services (DABS) agrees with these recommendations. We appreciate the care that the state auditors office took to investigate and review this matter when we brought it to their attention. As noted in this finding, the DABS took swift action immediately upon learning of the issue. The individual suspected of being responsible no longer works for the department and the department notified both the Auditor's Office and the Attorney General's Office. At this time DABS is waiting for the AG's Office to determine their next course of action.

The DABS updated the change order procedure (PR09-03) to provide clear guidelines on orders and verifications. DABS will continue to review and make additional updates as needed. Additionally, DABS

² Office of the Utah State Auditor Report No. 24-01, Finding #1, May 2024

has adjusted the bank reconciliation process to provide faster reconciliation which will assist in identifying potential issues.

Finding 2. Missing Store Sales Revenue Funds

For the period January 2021 to June 2024, we identified six currency short transactions totaling \$8,671 related to store sales revenue deposits. This indicates that the cash submitted to the bank was less than that documented on the deposit slip (see background section above). Two of these transactions totaling \$5,500 occurred at the subject Store in Finding 1, with the remaining transactions occurring at various other DABS stores.

DABS could not explain or account for the missing store sales revenue funds. The missing funds were not detected because DABS was not performing timely bank reconciliations. DABS has since improved its bank reconciliation process and appears to be able to address such discrepancies in a timely manner.

Recommendations:

We recommend DABS:

- Follow up with applicable store personnel when significant currency short transactions occur.
- Work with the Attorney General's Office to pursue additional criminal investigation.
- Consider seeking reimbursement from responsible individuals.

DABS' Response:

The Department of Alcoholic Beverage Services (DABS) agrees with these recommendations. We appreciate these recommendations and the care the state auditor's office took to investigate and review this matter when we brought it to their attention. The DABS has adjusted the bank reconciliation process which allows for faster identification of cash over short issues. DABS will also be working to adjust the policy (09-03) when issues are identified.

Finding 3. Change Order Policy and Controls Still Need Improvement

Following the discovery of the potential misappropriation of funds noted in Finding 1, DABS strengthened its policies and controls to prevent and detect similar activities in the future. DABS updated its change order policy to require additional documentation, which must be retained for seven years; however, the revised policy does not address Deposit timing. Statute requires that each State

agency shall “...deposit daily, if practicable, but no later than once every three banking days, all collections of state money...”³

The DABS change order policy should require Deposits be made within the statutory timeframe after the receipt of the associated Shipment. The lack of time requirement for the return Deposit increases the risk that change funds will not be returned appropriately and makes independent review of the change orders more difficult.

In addition to improving bank reconciliations, DABS implemented a separate change order reconciliation to ensure that Shipments are returned to the bank in their entirety. While these processes can greatly reduce the risk of change order related theft, we noted the change order reconciliation was not functioning as intended. The reconciliation contained inaccurate amounts that did not match supporting bank statements and DABS did not further investigate some unreconciled items. If DABS is not using accurate data and investigating discrepancies, it cannot reliably detect and address potential change order theft. While DABS should improve its change order reconciliation process, there did not appear to be any undetected theft as a result of the issues noted.

Recommendations:

We recommend DABS:

- Expand the change order policy to include a requirement that Deposits be made within the statutory timeframe after receipt of the related Shipment.
- Ensure that change order reconciliations contain accurate information.
- Promptly investigate any change order related discrepancies.

DABS' Response:

The Department of Alcoholic Beverage Services (DABS) agrees with these recommendations. DABS has adjusted the change order procedure (PR09-03) to account for the information received from audit partners and is being implemented. DABS is also evaluating the functionality of more robust cash management reporting with its current Enterprise Resource Planning (ERP) system capabilities.

³ UCA 51-4-1(2)

Background for Findings 4-6

Type 5 Package Agencies (Type 5 PAs) are contractually authorized to sell their own manufactured liquor directly to the public for off-premise consumption. These liquor sales are still subject to statutory earmarks for the Uniform School Fund⁴, the Public Safety Fund⁵, and Underage Drinking Prevention.⁶ DABS requires Type 5 PAs to remit a portion of their sales proceeds to pay for these earmarks and also a DABS administrative fee.

Findings and Recommendations 4-6

Finding 4. DABS Incorrectly Accounted for Type 5 Package Agency Liquor Sales

DABS should record revenues and expenses for liquor that it directly sells to licensees, PAs, and the public. Because Type 5 PAs do not purchase their liquor from DABS for resale, DABS should not record any revenue or expenses for these sales. DABS should only account for transactions that they are directly involved in, which are earmark funds and the administrative fee collected from Type 5 PAs.

DABS has been improperly recording sales revenue and expenses for Type 5 PA liquor sales, and overstated both accounts. This issue was discovered during the fiscal year 2024 financial audit cycle. After it was brought to their attention in September 2024, DABS discontinued the practice. At that point, DABS had already improperly recorded \$3,362,514 in expenses and \$3,846,619 in sales revenue for fiscal year 2025. DABS needs to ensure that these overstatements are corrected before the fiscal year-end closeout.

Recommendation:

We recommend DABS ensure that it reverses accounting entries made for Type 5 package agency liquor sales before the fiscal year-end closeout.

DABS' Response:

The Department of Alcoholic Beverage Services (DABS) agrees with this recommendation. DABS is working to analyze all entries related to sales and statutorily required transfers amounts and confirm

⁴ UCA 32B-2-304(6)(a)(ii)

⁵ UCA 32B-2-304(6)(a)(i)

⁶ UCA 32B-2-304(6)(a)(iii)

the accurate totals and adjust all entries. DABS did identify this concern in September of 2024 and prevented any entries from occurring since that time. The period from July 2024 through August 2024 is all that remains to be adjusted.

Finding 5. DABS Improperly Accounted for Statutory Earmarks

Type 5 PAs report their liquor sales to DABS through monthly sales reports. DABS uses these sales reports to calculate the amounts of earmarks and administrative fees to collect. DABS then records journal entries in D365 to account for the amount collected and allocated to each category.

DABS transfers money to the Uniform School Fund and Public Safety Fund on a monthly basis. There is no transfer of funds for the Underage Drinking Prevention earmark, which is a DABS operated program. DABS tracks the money internally and directs the use of the funds to the program. The cash flow associated with earmark collections related to Type 5 PA liquor sales should match the accounting, but we noted that this is not always the case as DABS calculates the cash transfer amounts independently. We noted issues on both cash transfer and accounting entries for these earmarks as described below.

Improper Fund Transfer Calculation:

DABS did not appear to properly calculate the fund transfers based on actual Type 5 PA liquor sales. Based on Type 5 PA fiscal year 2025 sales reports through January 2025, the earmarks were initially underfunded. Partway through our audit, DABS made an adjustment and has now overfunded the earmarks for fiscal year 2025. The following table shows the amount that the earmarks were over or under funded prior to the adjustment and after.

Earmark	Initial Amount Over/(Under) Funded	Amount Over/(Under) Funded After Adjustment
Uniform School Fund	(\$634,637)	\$126,571
Public Safety Fund	(\$107,571)	\$21,454

Improper Accounting:

DABS was not properly tracking and accounting for funds collected from Type 5 PAs. Our audit reviewed entries for seven months in fiscal year 2025; for five of those months DABS booked the entries incorrectly. In addition, DABS made several incorrect adjusting entries that impacted the account balances. The following table shows the amounts over or under booked to these accounts.

Earmark	Amount Over/(Under) Booked
Uniform School Fund	(\$9,922,737)
Public Safety Fund	(\$43,754)
Underage Drinking Prevention and Administrative Fee	\$1,824

None of the entries booked were subject to a formal review and approval process. Had D365 required reviews and approvals prior to recording entries, DABS may have detected and prevented these errors (see Finding 7). Proper accounting is crucial for financial reporting and ensuring that earmarks are properly funded.

Comingled Accounts for Tracking Earmark:

DABS tracks the Underage Drinking Prevention earmark and the administrative fee in the same miscellaneous income account, making it difficult for DABS to determine which funds should be allocated to the earmark. DABS should track this earmark in a separate account.

Recommendations:

We recommend DABS:

- Ensure the correct funds are transferred to each earmark.
- Ensure each earmark is properly accounted for.
- Track the Underage Drinking Prevention earmark in a separate account.

DABS' Response:

The Department of Alcoholic Beverage Services (DABS) agrees with this recommendation. DABS has generated additional revenue source codes in conjunction with the Department of Government Operations Division of Finance to provide clarity and assist in monitoring totals as presented by Type 5 Package Agencies. DABS is also adjusting team member responsibilities to provide greater oversight in the review of financial transactions and reporting.

Finding 6. DABS Did Not Ensure Accuracy of Type 5 PAs Monthly Liquor Sales Report

Type 5 PAs self-report their liquor sales data to DABS through monthly sales reports. DABS performs annual audits of each Type 5 PA, but these audits are primarily focused on other statutory compliance. As part of its audit, DABS ensures that the Type 5 PA has a functioning point of sale (POS) system that

can properly export sales data. However, DABS does not ensure that the submitted sales reports match this POS data. As a result, Type 5 PAs could misreport their liquor sales without detection, resulting in DABS not collecting the proper funds for statutory earmarks and the administrative fee.

Recommendation:

We recommend DABS establish audit procedures to ensure that Type 5 PAs are accurately reporting liquor sales.

DABS' Response:

The Department of Alcoholic Beverage Services (DABS) agrees with this recommendation. DABS is strengthening its oversight and accountability with Type 5 PAs by adjusting team member responsibilities to create a subject matter expert with a focus on the reporting and monitoring of all package agency financial information.

Background for Findings 7-9

DABS operations are an integral part of the State's financial operations. DABS annually transfers excess profits to the State's General Fund⁷ to be used for other public expenses and public works⁸ as required by statute. In addition, DABS is reported as a major proprietary fund in the State's Annual Comprehensive Financial Report (ACFR). The ACFR facilitates transparency and oversight of the State's use of public funds and is used for bond reporting requirements. Therefore, DABS's accurate accounting of its financial operations is crucial to the State's financial reporting. If DABS has not accurately recorded its operations by fiscal year-end closeout, it could delay ACFR preparation and issuance. DABS tracks its financial operations in its own accounting system (D365) and is required by state policy to transmit its financial operation data to the State's accounting general ledger system (FINET). DABS implemented D365 in October 2022, and since encountered difficulties transferring its data into FINET.⁹

⁷ The General Fund is the State's principal operating fund.

⁸ UCA 32B-2-301(6)(a)

⁹ Office of the Utah State Auditor Report No. 23-01, Findings #1 and #2, July 2023 and Office of the Utah State Auditor No. 24-01, Finding #1, May 2024

Findings and Recommendations 7-9

Finding 7. Lack of Approval for Accounting Entries and Previous Fiscal Year Not Closed Out

DABS does not require a formal approval process to book accounting journal entries in D365. As a best practice, after an accounting system adjusting entry is prepared, someone other than the preparer should review and approve the entry before it is recorded into the accounting system. This practice helps detect and prevent inaccurate entries and reduces the risk of fraudulent entries. During the course of our audit, we noted several erroneous accounting entries that had been booked in D365 (see Finding 5 above). Having a formal approval process may have detected these before they were recorded. D365 has the functionality requiring a formal approval process, but DABS did not set it up when implementing the system. DABS has been considering instituting this approval process but has not yet taken action.

Additionally, DABS has not closed out fiscal year 2024 in D365. As a best practice, entities should close out fiscal years that have ended within a timely manner. This prevents further adjustments from being made after the accounting periods ended and have been audited. The closeout process also ensures that balance sheet accounts are properly rolled forward to the current fiscal year so that these account balances can be accurately presented in the current fiscal year.

Furthermore, both issues discussed above have the potential to adversely impact the State's financial reporting.

Recommendations:

We recommend DABS:

- Ensure journal entries are reviewed for accuracy prior to recording in D365.
- Set up D365 approval function.
- Close out fiscal year 2024 in D365.
- Establish and follow a policy to close out future fiscal years in a timely manner.

DABS' Response:

The Department of Alcoholic Beverage Services (DABS) agrees with these recommendations. DABS recognizes the issue related to closure of the fiscal year and is implementing new procedures to prevent the issue from occurring in the future. Additionally, DABS is working to enhance the approval workflows for the D365 system to provide checks and balances.

Finding 8. DABS Operations Not Recorded or Reconciled in the State's Accounting System in a Timely Manner

As mentioned in the background section above, DABS is required to transmit its data from D365 to FINET. DABS should be transferring this data in a timely manner, at least monthly. When this data is not transmitted accurately or in a timely manner, it hinders proper oversight and can affect the State's financial reporting. As of mid-March 2025, DABS had not properly transmitted all data for the completed portion of fiscal year 2025. The following issues contributed to DABS's inability to properly transmit the data:

Improper Use of Clearing Accounts:

When transferring data into FINET, DABS historically would first transfer most transactions into two clearing accounts and then subsequently move them to the proper accounts. Moving the data from clearing accounts to the correct accounts requires additional work and is thus more prone to error. In the fiscal year 2024 financial audit cycle, improper clearing of these clearing accounts resulted in a significant adjustment to the State's ACFR and to the liquor profit transfer.

As a result, in October 2024, DABS finance personnel altered the process to transmit data directly to the correct accounts in FINET, rather than to clearing accounts. As of the time of our audit fieldwork, DABS had transmitted the data for October 2024 through January 2025 in a timely manner using the new process. We were able to validate that this data was transferred correctly. However, the data for July through September 2024 was still in clearing accounts at that time. DABS is in the process of reversing these initial transfers and using the updated method to transmit data for these months but has not yet completed it. DABS needs to ensure that the July through September data and remaining months of the fiscal year are properly transmitted to FINET before the fiscal year-end closeout so as not to hinder the State's financial reporting process for the current year.

Transmission Process is Manual and Impractical:

D365 has the capability to interface directly with FINET to automatically transfer data. While DABS intends to utilize this functionality, it has not yet activated the function. As of April 2025, DABS finance personnel still transmit the data manually. The current process of preparing the data for transmission is time intensive and complex. DABS uses a basic spreadsheet program, which struggles to compute large quantities of data. The sheer numbers of transactions in DABS' data transmission frequently causes the program to crash. If DABS were to utilize a data analytic software, it could streamline the process, enhance efficiency and reduce the risk of errors.

No Formal Reconciliation:

Even though DABS had transmitted data for October 2024 through January 2025 as described above, as of April 2025, DABS had only performed a formal reconciliation for the October 2024 data. Given

that the current data transmission process is manual and prone to error, DABS should be performing regular reconciliations, at least monthly, between the data in D365 and FINET to ensure all data is transmitted to FINET properly and, if applicable, to address any discrepancy in a timely manner.

Recommendations:

We recommend DABS:

- Ensure that all D365 data is recorded in FINET and reconciled in a timely manner.
- Resolve system interface issues to automate the data transmission process.
- Consider utilizing a data analytic software to streamline the data transmission process.

DABS' Response:

The Department of Alcoholic Beverage Services (DABS) accepts these recommendations. DABS acknowledges that the transmission process is manual and impractical. Since receiving funding in July 2024 to address these systems issues, DABS has made substantial progress on the development and implementation of a sustainable, long term solution. Concurrently, with new finance leadership and a collaborative approach with state and intergovernmental partners, DABS and DTS are developing short term and immediate solutions.

DABS has adjusted the process by which transactions are transmitted to the state system (FINET) for a more formal process. In addition to that process change we added a reconciliation process. At the time of this response, DABS has transmitted all periods except March 2025, given the 30 day lag from the close of a period to the completion of transmittal, and has reconciled the majority of periods to the FINET system. DABS is also working on an automation process to prevent delays in transmittal and reconciliation.

DABS has also ceased the use of the clearing account process to prevent issues in reporting. This process has been reviewed by the Office of the State Auditor (OSA) and is currently being reviewed by an external CPA firm. This change will ensure faster processing and transparent reporting and is complete for all completed periods in FY2025.

Finding 9. DABS Unresolved Accounting Problems with COGS

During the fiscal year 2024 financial audit cycle, DABS had misreported Cost of Goods Sold Expense (COGS)¹⁰ resulting in several significant adjustments to the State's ACFR. COGS is one of the

¹⁰ Cost of Goods Sold represents the direct costs associated with producing or acquiring the goods an entity sells.

components in the calculation of the annual liquor profit transfer (see background section above). If COGS is misreported, it will impact the amount of money transferred to the General Fund that is available for other public expenses and public works. In response to COGS adjustments, we designed our audit to include various procedures that assessed the accuracy of COGS. One of the procedures performed was to recalculate COGS for the first half of fiscal year 2025 using the following formula. All inputs were pulled from D365.

Cost of Goods Sold Expense (COGS) = Beginning Inventory + Inventory Purchases – Ending Inventory

This formula is a standard calculation that represents the relationship between COGS and inventory. Any deviations from this formula could be indicative of accounting or system problems. Based on the formula, COGS should be \$13 million (or 8.25%) higher than what DABS recorded in D365 for the first half of fiscal year 2025.

As of April 2025, DABS was unable to explain this discrepancy and is currently investigating the issue. If this issue is not resolved before the fiscal year-end closeout, it could have a major impact on the State's Annual Comprehensive Financial Report (ACFR) and the liquor profit transfer, potentially influencing State budget decisions. We consider this to be a significant unresolved, open issue as of the date of this report, and we will continue to monitor it to ensure DABS resolves the problem by the end of fiscal year 2025.

Recommendation:

We recommend DABS continue investigating and prioritize resolving the COGS discrepancy.

DABS' Response:

The Department of Alcoholic Beverage Services (DABS) continues to be dedicated to the research needed to determine the cause of concern with the COGS. At present, DABS has completed a full inventory count and has hired an accounting firm to assist in an analysis of the calculation and process. DABS will continue to share any findings as the process continues.