

BOARD MEETING MINUTES:

March 27, 2024
ABC Headquarters

Call Meeting to Order

Board Chair Tim Hugo called the meeting to order at 9:00 a.m.

Attendees

Board Chair Tim Hugo
Board Vice Chair Dale Farino
Board Member Greg Holland
Board Member William Euille
Board Member Lisa Jennings
Chief Government Affairs Officer, John Daniel
Chief of Law Enforcement, Tom Kirby
Chief Retail Operations Officer, Mark Dunham
Chief Administrative Officer, David Alfano
Chief Information Officer, Paul Williams
Deputy Secretary, Chris Curtis
Office of the Attorney General, Jim Flaherty
Director of Finance, Doug Robinson
Tony Lee, Chief Transformation Officer, Governor's Office
Executive Assistant, Kathleen LaMotte
Senior Paralegal, Helen Gordon

Opening Remarks

Board Chair Tim Hugo asked Interim CEO Kirby to provide the agenda for today's meeting.

Mr. Kirby stated that the agenda has an update by Paul Williams (IT), approval of the Real Estate Committee (REC) recommendations, a closed session to discuss legal advice from counsel, a hearing at 10:00, a review of Authority financial information, but that the agenda can of course be reversed if the Board wishes.

Board member Euille advised he prefers to adhere to the posted agenda.

Approval of Minutes

The board reviewed the minutes from the February 21, 2024 board meeting. Mr. Euille moved to accept the minutes; Board Member Holland seconded the motion. The motion passed on a roll-call vote of 4 – 0, with Board Member Jennings abstaining from the vote.

Comments from the Chair

Mr. Hugo asked Mr. Alfano regarding a statement in the February minutes that all spending requests over \$10,000 were reviewed by the CEO. Mr. Hugo asked what the previous cap was for review. Mr. Alfano responded that while there had not been a cap previously, there were always checks and balances in place. There is now an added step brought in by Mr. Kirby when he began as Interim CEO that has proven to be helpful and understand spend. This provides an additional level of discipline, a second set of eyes on all spending over \$10,000. The Chair asked if there was a level of

spending that came before the Board, Director of Procurement Melissa Watts advised that a spend in excess of 1.5 million must be approved by the Board.

Mr. Hugo shared a note from industry partner Sazerac in support of interim Chief Kirby.

Strategic Plan

Chair Hugo asked for Mr. Kirby to update the Board on the Authority's strategic plan.

Mr. Kirby stated that a strategic plan was developed in the summer of 2023, however the plan didn't align with the direction of the Authority as set by the budget approved in August of 2023. Expansions into digital and e-commerce were shelved, and the strategic plan was not put before the Board and must be re-worked to focus on the Authority's current priorities.

Mrs. Jennings stated she would like to review the Authority's current strategic plan and any previously developed plans.

Mrs. Jennings and Mr. Farino will arrange for a time to come in for an orientation, and Mrs. Jennings advised she would like to review the strategic plans and financial information in advance of that meeting to develop her questions. Mr. Farino would like for Tony Lee of the Governor's CTO office to attend the session as well.

IT Update:

Paul Williams, Chief Information Officer, reported that:

The Authority is required by statute to provide an update of on the status of financing, procuring and implementing the information technology systems necessary to sustain the Virginia Alcoholic Beverage Control Authority's business enterprise. The most recent report was provided to the Board, along with an IT overview and an IT Strategy document previously presented at the December 2022 Board Meeting.

While the Authority is in a much better position than in previous years, there are some remaining legacy issues.

The Authority has an average uptime of 99.9% reliability, much higher than when the Authority was supported by VITA.

Mr. Hugo asked if IT reviews the technology used in the Distribution Center. Mr. Williams stated that his team handles the contracts for the warehouse, and handles computers and printers, but the conveyors were managed by Susan Johnson and the Real Estate/Facilities team.

Chair Hugo asked if there was a technology upgrade when we moved here from Hermitage. Mr. Williams replied that it was a huge upgrade as the Hermitage Road facility was far behind technologically.

Mark Dunham, Chief Retail and Operations Officer, spoke to the Board's questions regarding DC efficiency, benchmarks, and comparisons between the old and current facilities.

Mr. Williams continued:

IT has incurred some costs that are more of a spend at the front end, but eliminates future spending as the Authority moves to a more cloud-based, software as a service model. This eliminates an ask for more money to replace systems based on-site as they reach end of life.

The Authority now hires more configuration managers for program analysis than developers.

In response to Mr. Hugo's inquiry about the storage of credit card data, Mr. Williams responded that the ABC endeavors to make itself a poor target for hackers. The Authority has not stored credit card data in-house for over four years. If a credit card does not work at the point of sale, there is not a method to manually key-in the credit card information or hold the number on site at a store. Credit card information is stored by a vendor.

The Licensing software system (VAL) contains some sensitive information such as social security numbers, but this is also hosted in the cloud by a vendor.

Mrs. Jennings asked about the purchase of high-end laptops if the Authority had considered the use of thin client systems where appropriate versus the purchase of high-end computers. Mr. Williams replied that the Authority is reliant on workers being able to work from home, and in the event of a disaster there is only one headquarters and the ability to work remotely is part of the Authority's Continuity of Operations Plan. These machines have a longer battery life, break down less often, and do not need to be replaced as often as less expensive machines. The authority's complaint volume is down 40 – 50% since handling our own IT, and maintenance costs are below budget.

Mr. Hugo thanked Mr. Williams and his staff for their work on this.

Real Estate Recommendations:

Mr. Kirby directed Chairman Hugo and the Board to look at page 57 of their Board books to review the REC recommendations. Of note, the committee advises the Authority to close store 154 in Danville effective May 31, 2024. There are three other stores in Danville, and the committee decided that it was risky to remain in that location, as the landlord is non-responsive to the Authority's requests to replace the roof, does not pay taxes, and doesn't cash rent checks from the Authority.

Mrs. Jennings said in the annual report it appears that there are other stores with a negative annual return, and that it may be timely to renegotiate leases given the stress in the commercial real estate market. Susan Johnson, the Director of Real Estate and Facilities, advised that some stores remain open as part of the Authority's mission to provide spirits to all areas of Virginia, as some rural consumers may have to drive over an hour. Mrs. Johnson advised that all stores still provide tax revenue and none are totally in the red.

Mr. Kirby advised that an analysis could be done on underperforming stores, some may change footprint or staffing, not necessarily close.

Tony Lee of the Virginia CTO office advised that the Authority's annual report speaks to the "four wall" revenue of the store, but there is another element and calculus of the tax revenue and sales tax that is not reflected in the annual report.

Mr. Holland asked if legislators still considered it a boon to bring an ABC store to their area. Mr. Williams reported that local politicians were very excited to welcome ABC to the Jonesville area, as the county was dry for many years.

Board Member Euille moved to approve the recommendations for the closure of store 154 (Danville) and the renewals of stores 053 (Windsor), 084 (Fairfax), 143 (South Hill), 219 (Fairfax), 390 (Montpelier) and 439 (Prince William). Mrs. Jennings seconded the motion, and the Board adopted the recommendations of the REC on a roll call vote 5 – 0.

Chair Hugo asked for an update on store 361 in Portsmouth. Ms. Johnson advised that this was the top store in the state for retail theft, and a shooting (unrelated to ABC) occurred in the parking lot outside the store. The Authority looked into several options; breaking the lease was not an option and the Board approved converting this location to a counter store. Sales may have gone to other ABC stores, or to neighboring grocery stores for beer and wine vs. traveling further for spirits.

Mr. Alfano stated those counter stores have only been open for a short while, more time is needed prior to completing an analysis to see how they are performing.

Chair Hugo stated that we want to make sure we are maximizing all possible reductions during this budget analysis time.

Mr. Kirby explained the problems at store 361 and the decision to reopen it as a counter store. Store 110 became a counter store as well after another analysis of that store as requested by the local police. The Authority has five counter stores in total.

Mr. Holland asked if having police patrols around the stores to help with safety had been discussed?

Mr. Kirby replied that we have done some joint task forces with ABC agents and local police agencies to see what we could do to try to prevent larcenies, however, not every jurisdiction is open to try this. Norfolk is willing to try many

different things to see what can help to reduce theft, even placing an officer in a store. When this was done though, the theft just moved to a different store.

Closed Session

At 9:50 a.m., Mr. Euille moved that the Board enter closed session pursuant to Virginia Code §2.2 37.1(A)(7)(8) to receive the advice of counsel regarding actual or probable litigation. Mrs. Jennings seconded. The motion passed on a roll call vote of 5 – 0. Attending the closed session in full were Tim Hugo, Dale Farino, Greg Holland, William Euille, Lisa Jennings, John Daniel, Jim Flaherty, and Tom Kirby.

Appeal Hearing (Fidel Restaurant)

Return to Open Session:

When the Board returned from Closed session at 11:15, Mr. Holland moved to certify that to the best of his knowledge nothing was discussed in the closed sessions but advice of counsel regarding actual or probable litigation pursuant to §2.2 37.1(A)(7)(8), and only public business matters lawfully exempted from open meeting requirements was discussed. Board Member Euille seconded; the motion passed on a roll-call vote of 5 - 0.

Chair Hugo asked if there were any questions on the C-Suite updates in the Board books?

There being none, Chair Hugo asked Mr. Kirby and Mr. Alfano to move into the financial update.

Financial Update:

Chief Kirby referred the Board to the handout. These sheets attempt to answer some of the questions raised by the Board last week regarding the GACRE forecast. The numbers presented today are the same but have additional detail into the numbers.

Mr. Hugo said we had a special session last week due to some inquiries from the governor's office. Do we need to take a vote today on the governor's inquiry? Mr. Kirby responded that he was not asking for a vote today. Based on the last meeting the Authority provided the preliminary figures were posted publicly, the information from today will also be posted publicly.

Chief Kirby reviewed decreases in the consulting budget, while there is some spend in FY24, this was prior to the FY24 budget being approved by the board in August of 2023 and occurred in July of 2023. Most of the contractual staff was a contractor supplementing hard-to-staff IT roles.

Mr. Holland asked Mr. Williams how difficult it has been with this budget to maintain IT's fine level of service? Mr. Williams stated continuity and ability to sustain is ok, but challenging. IT is slightly less responsive and has lost the capability to execute major projects. IT has not been able to resolve all the bugs and backlogs and provide needed enhancements. IT has not been able to alter the HR system to support annual reviews. Lottery releases, improving two-factor authentication, and improvements to the MIPS, tax management and account central programs have all been pushed aside. The IT staff continues to work as best they can to meet the needs of the Authority. Defenses to AI are not where we need them to be. There will be a lot of changes over 7 – 8 weeks for new release of the point-of-sale upgrade. There is a fixed budget for upgrades to the VAL system but other systems are running slowly in terms of upgrades..

Chair Hugo stated that Member Holland brought up a good point. We need to keep looking at the budget now and towards the future. The Chair acknowledged that he has investigated some of these items and that he hears what is being said about the budget. However, he has to say that he thinks the current Governor's administration has done a good job of sending people in here to look at the budget. We've already reduced the amount of money spent on bags; we have two savings on the Chiefs' level; not even counting benefits for those positions that no longer have to be paid. From 2017 to 2023 there was a huge explosion in salaries on the executive level; their salaries were quadrupled.

Contracts for Thought Logic and Singlestone added up to \$2.3 and \$3.2 million respectively. Chief Kirby noted that the Authority has cut \$10.9 million additional dollars.

Chair Hugo asked if anything had been lost with the leaving of the two chiefs? Chief Kirby said other C Suite members have absorbed their duties, and the Authority is also not replacing the position of a director that left state service.

Chair Hugo stated that IT is expensive, and we need to look at IT to make sure it's cost efficient. For example, spending \$5 million more on bags seems extravagant, and the level of spend on contractors seems extravagant. The Authority has cut nearly \$11 million without looking like they are breaking a sweat.

Chief Government Affairs Officer John Daniel advised that the over-budget spending on bags was due to a mandate by Executive Order of the previous Governor, which was in effect until rescinded by the current Governor. The spending was not due to inefficiency by the Authority, but due to a legal demand.

Chief Kirby said there has been a lot of conversation on the net profit. The Authority has taken a different leadership approach and has put control measures in place that have limited the amount of loss despite lower sales.

Member Euille asked if the current forecast for fiscal year 2024 was a revision? Chief Kirby replied that it was and reflects a downward turn in expected revenue.

Board Member Farino said I think one thing we need to look at is that we need to maximize the income. We can't continue to have years where our operating expenses are more than the income. Mr. Farino asked about manpower budgeting. Mr. Alfano replied that the Authority is reviewing each division's true attrition rate, how long it takes to fill a position, etc. IT and Enforcement vacancies often take longer than three months to fill. We will continue to build these forecasts in our budget.

Chief Kirby said that when he assumed this role, he realized that revenue was going down and it wasn't matching our budget, so he started trying to mitigate the damage. He has succeeded in getting that deficit down to 4.9 million, but is disappointed that he couldn't meet the amount we needed. However, if we hadn't taken steps to try to mitigate the damage, that number would be much worse.

Chief Kirby gave the example of discount tags in stores. We're spending six figures on printing tags. Do we have to have that special printed tag to draw the customer's eye? The team is going back to see if there is anything else we can do. Mr. Farino recalled that ABC used to hand-write price changes, and the prevailing opinion was that it was making the stores look disorganized, and that's why there was an investment made in printed tags. Mr. Kirby responded that was correct, however we are trying to find a balance.

Mr. Alfano added that we are seeing the effects of the discipline being applied, and this will continue going into the next budget cycle.

Chief Kirby stated that his leadership style is different than the previous CEO, and the new CEO will probably have a different leadership style. Mr. Kirby stated he strives for transparency and doesn't want to lose personnel and talent. The Authority is changing the way it looks at spending money, and thinks we could still have top-rated stores, but could do this with a better profit margin.

Mr. Holland stated that he appreciates ABC's work, and that all have done a fantastic job across the board. He recalled sitting around this table having a frank discussion that we were going to lose a good proportion of our people because we weren't paying them enough. There was no disagreement raised to that. The main reason we are where we are is that we had to increase what we paid our people across the Board. It was mandated that we had to increase the pay across the Board, to include our executives, because otherwise we were going to lose them. These are hard decisions and we made hard decisions 2 ½ years ago. We have at least managed to become a quasi-state agency. We will lose good people to private industry where they will be paid better. We've got to take that into consideration.

Mr. Alfano agreed that it's a balancing act. We do have to look at pricing our jobs appropriately, so we are getting the quality candidates we need. We need to make sure we aren't overpaying people, but we also don't want to make it so low that we're not getting the level of quality/talent that we want.

Mr. Kirby reiterated that our number one asset is our people. I want to invest in our staff. I do believe that we have some of the best employees in the State of Virginia, private or public.

Mr. Hugo agreed that you do get what you pay for, but it is a balancing act as well. You did go down in the number of directors and chiefs but yet you're still managing to operate. Mr. Hugo thanked the Authority for taking a look at this.

Mrs. Jennings gave several examples of things for the Authority to look at, such as more sophisticated modeling techniques, turning in cars to the state, charging for bags, combining vendor contracts, and do more to recoup costs. Mrs. Jennings also expressed concern regarding advanced buys. Mrs. Jennings observed that the major variance impacting sales with the mix of product, offsetting the positive variance in product sold and suggested that a volume/mix projection model would be beneficial to widen the spread from sales.

Mr. Alfano stated that for 2025 and 2026 this is a very high level, quick estimate. The Authority will do a more in-depth budget and go through this exercise over the next three months. The Board will receive a department-by-department count. Mr. Alfano added the Authority runs on a bailment system, and product in the DC is not owned by the Authority until it is shipped to stores, with the exception of taking advantage of advance buys prior to a known price increase from the manufacturer.

Doug Robinson, Director of Finance, stated that the Authority examines the turnover and only pre-purchases products that would turn in less than 90 days when we do advance buys. We do not buy items that are just going to sit on our shelves for months. The Authority does get a return and it's normally \$400,000-\$500,000 in savings.

Mr. Dunham added that on the risk side, we are buying at a lower price, but the goal is that we are through that product before the next quarter rolls around. Mrs. Jennings agreed that pre-purchase could be a natural hedge to pricing variances but should be considered in conjunction with a financial pricing model that includes an analysis of price and income elasticities. The Authority team responded that there are no internal models used for pricing and that any work in that area would be performed at the Administration.

Tracey Heilborn, the Director of Spirits Supply Chain, also added that the effect on the profit is that we won't have to replace that stock. The Authority is also examining bringing back items from stores that are not selling to the DC to send to other ABC stores where they sell better. Currently, the bailment inventory is higher than normal.

Mr. Alfano went on to say that ABC's Internal Audit is actively looking at the state cars and is going to put forth recommendations on them. Efforts are underway, with an exception for Enforcement cars. Anticipates that the Authority will have fewer cars and have a pool vs. individually assigned cars.

Mr. Farino asked if the Authority paid a car allowance. Mr. Alfano responded that drivers receive a mileage reimbursement. Agents have cars, retail managers that go out to stores constantly have cars but other divisions do as well.

Chair Hugo said that he had talked to Chief Kirby previously about the Governor's restriction on travel as well as about the rental of the building. Is there any update on that? Mr. Alfano said he would inquire with DGS about an update. The Governor's CTO, Tony Lee, advised that he would also look into the matter, as this would definitely be a cost-saving help to the ABC.

Mr. Holland said that he is not opposed to cutting costs but is concerned about retail over-allocation of hours in January and last July and August. There must be some responsibility for that. Mr. Alfano said that this is getting under control with the help of a workgroup.

Mr. Kirby said that the Authority did have the overspend that Mr. Holland indicated. In turn, the Authority now has a team of district managers that is working to come up with a sustainable allocation model for our stores. The lack of tools

to measure the allocation of workers in stores was part of the problem. The hours required to run a store is offset by short term disability, time off, and special sales. Forecasting the needs for these circumstances wasn't done. The Authority is asking retail to re-do how they do staffing in stores. The manager doesn't have any real type of system to manage time. Stores have different hours and different volumes. Feedback has been positive from people in the field and in this room.

Mr. Robinson added that with the tool in their hands, there should now be no excuse to go over on hours. The tool allows greater oversight to constantly monitor hours.

Mr. Kirby said that we do believe in accountability. I don't know how you could operate the retail division without this type of management. It's in training the district managers and the store managers in doing things differently.

Mrs. Jennings said what I didn't hear about the tool, does this account for the traffic in each store? All of that should be captured in time stamps, etc. Most retail stores that are profitable over their peers employ these models. It is not always the best practice to push the ability to define hours to the stores.

Mr. Kirby replied that that was a very valid point. January was dismal from a revenue viewpoint and then some stores were closed for several days for weather, which exacerbated the poor sales numbers.

Mr. Hugo asked if Member Jennings had gotten everything she wanted on the aggregate contracts? Mrs. Jennings stated she would still like to see more information. Mr. Hugo asked if Mrs. Jennings received the information she requested in the previous board meeting, including on aggregate contracts. Mrs. Jennings replied that she did not and was still waiting for the strategic plan and five year financial statements. Mr. Alfano said that his team was getting that information together for Mrs. Jennings.

Mrs. Jennings remarked considering the size of the expense from interchange fees on credit cards, did the Authority have the ability to add the fees as part of the bill. asked about getting something in place to charge for credit card fees as many restaurants do. Mr. Curtis said that will need additional review. unfortunately, Code Section 4.1-240 limits what we can capture from credit card charges.

Mr. Euille asked what needs to be done with this most recent forecast. Mr. Kirby responded that the Board doesn't need to do anything right now. The Authority will start our budget process and will want the Board to provide input on that. The Board will see the budget sometime in May/June.

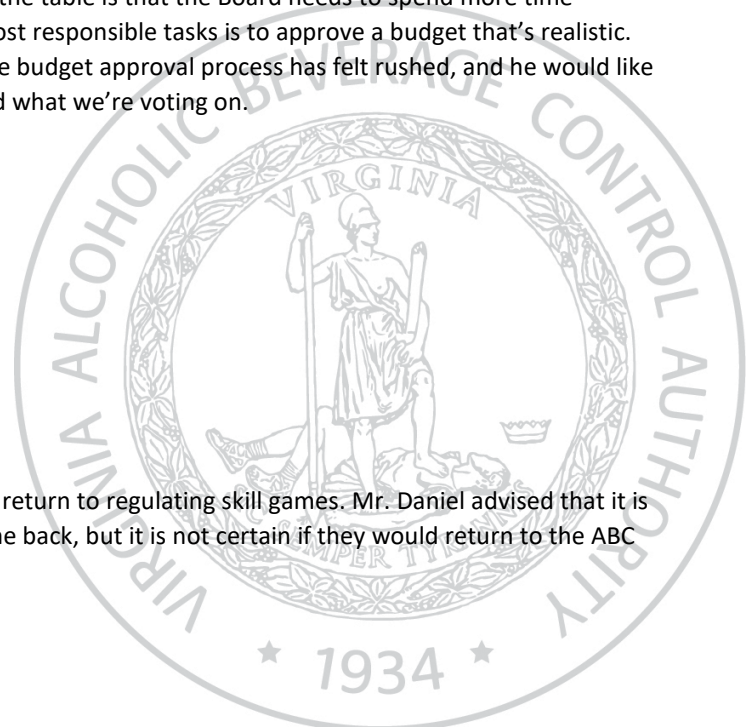
Mr. Euille stated that he believes what he's hearing around the table is that the Board needs to spend more time working with the staff on the budget. One of the Board's most responsible tasks is to approve a budget that's realistic. Mr. Euille advised that in his first 2 ½ years on the Board, the budget approval process has felt rushed, and he would like to have the time to really look at the figures and understand what we're voting on.

Public Comment

No comments received.

Board Comment

Mr. Holland asked if it was certain that the Authority would return to regulating skill games. Mr. Daniel advised that it is not decided at this time. Mr. Hugo believed they would come back, but it is not certain if they would return to the ABC or return to another agency.



Closed session

At 12:30 pm Mr. Hugo moved that the Board convene into closed session to receive advice from legal counsel pursuant to Virginia Code § 2.2-3711(A)(7) to discuss actual or probable litigation. Attending the closed session in full were all Board members, Chris Curtis, John Daniel, Tom Kirby, Dave Alfano and Jim Flaherty. Mr. Euille seconded the motion, and the motion passed on a roll call vote of 5 – 0.

Return to Open Session

When the Board returned from Closed session at 2:00 pm, Mr. Hugo moved to certify that to the best of his knowledge nothing was discussed in the closed sessions but legal advice and counsel on probable or actual litigation pursuant to §2.2 37.11(A)(7), and only public business matters lawfully exempted from open meeting requirements was discussed. Mr. Farino seconded; the motion passed on a roll-call vote of 5 - 0.

Meeting Adjournment

Meeting adjourned at 2:00 p.m.

