

**REPORT TO THE LEGISLATURE
REGARDING ACT 1, SECTION 112 (SPECIAL SESSION 2018)
ON THE CONSOLIDATION OF THE DEPARTMENT OF LIQUOR
CONTROL AND THE VERMONT STATE LOTTERY**

**Submitted to the
Senate Government Operations Committee
House General, Housing & Military Affairs Committee
House Corrections & Institutions Committee
House Government Operations Committee
Senate Economic Development, Housing & General Affairs Committee
Senate Institutions Committee**

Department of Liquor and Lottery

January 14, 2019

Introduction

During the 2018 Legislative Special Session Act 1, relating to the consolidation of the Department of Liquor Control and the Vermont State Lottery into a single department was passed and signed into law. Section 112 of Act 1 directs the Department to prepare a written report on or before January 15, 2019, 2020, and 2021 regarding the Department's "success in carrying out the functions of the former Department of Liquor Control and the Vermont State Lottery. Specifically, identify any improvements in efficiency and customer service levels, as well as any savings or additional costs, that have resulted from the merger of the two entities. The report shall also provide detailed information regarding the Department's progress with respect to securing a facility that will meet its office and warehouse needs. In addition, the report shall include any recommendations for legislative action that may be necessary to effect the intent of this act."

1. Success in Carrying Out the Functions of the Former Department of Liquor Control and Vermont State Lottery

Pursuant to Act 1, The Department of Liquor Control (hereinafter Liquor) and the Vermont State Lottery (hereinafter Lottery) officially became one entity on July 1, 2018. At the time of the consolidation the top-level management team consisted of a Commissioner and a Deputy Commissioner at Liquor, and the Executive Director of the Lottery. The lottery executive director position transitioned to become a deputy commissioner position on July 1. In mid-August the Deputy Commissioner responsible for the operation of the lottery resigned. Shortly after his resignation the decision was made to assign the remaining Deputy Commissioner to be responsible for the day-to-day operation of the lottery.

This loss of a top-level manager created a number of challenges but also allowed the Deputy Commissioner who had two and a half years' experience at Liquor to identify opportunities for improvement in the consolidated department (discussed in the section that identifies improvements below). One of the challenges was that the existing work of three top-level managers was now being done by two. This challenge was further exacerbated by the fact that the two divisions operate out of separate offices five miles apart. Both divisions have major projects underway or in the request for proposal (RFP) phase. The Liquor division was starting the implementation phase of replacing the existing antiquated point-of-sale system. The first phase of the rollout of the new system had just commenced in August shortly after the consolidation become law. The Liquor division was also undertaking a major signage project for the retail stores and was also working on a request for information (RFI) for an on-line licensing system. The Lottery division was working on the creation of an RFP for a gaming system vendor. The contract with the existing vendor is set to expire after ten years in 2020. The RFP is for a ten-year contract with two five-year extensions for a possible twenty-year contract worth an estimated \$80-120 million. While all this mission critical work was taking place in the two divisions all the regular day-to-day business operations had to also continue uninterrupted.

I am happy to report that despite the many challenges (including numerous staffing issues¹) both divisions continue to function well. A great deal of this success is attributable to the dedicated and hardworking staff in the department. The staff recognized the challenges facing the department and rose to the occasion. It was also crucially important that Commissioner Delaney and Deputy Commissioner Kessler worked closely together over the last two and a half years at Liquor, as this experience allowed them to communicate and coordinate their efforts effectively despite now operating out of separate offices.

Of course, it is easy to claim that all is going well, so we have supported our claim with facts that make the case:

- Lottery sales are up \$3,352,000 (4.9%) over the same time period as last year.
- Liquor sales are up \$1,354,068 (3.37%) over the same time period as last year.
- Lottery instant ticket sales during the last week of December set an all-time weekly sales record of \$2,566,926.
- The Liquor point-of-sale project is nearly complete with sixty-seven stores on the new system with no significant issues which is highly unusual for such a complex IT project. The remaining eleven stores will be operating on the new POS system by the end of January.
- The Lottery gaming RFP was posted and is progressing on schedule.

In conclusion we believe that based on the information presented above that the new department has been successful in carrying out its required functions.

2. Opportunities for Operational Improvements as a Result of the Consolidation

An objective of this report is to “identify any improvements in efficiency and customer service levels, as well as any savings or additional costs, that have resulted from the merger of the two entities.” As it is early in the history of the consolidation there are few savings or additional costs to report. That does not mean that we have not been thinking and planning for changes that will improve customer service and create efficiencies. These ideas for change are laid out below:

- The two entities each had a staff member whose duties included human resources. With the retirement of one of those staff members the Department will have one HR person for the seventy-six staff members going forward. This will result in small payroll savings, but we plan to reallocate the vacant position to fill a needed financial services role at Lottery.
- The Lottery has a single person responsible for security. This includes internal security matters as well as compliance checks at the 630+ lottery agents. The security staff member is also responsible for supervising lottery warehouse staff and helping in that area when there is high demand, or when a staff member is out. As a result of the consolidation, we have paired the Lottery Security Director with the Liquor Director of the Office of Compliance and Enforcement. They have already worked together to develop a tracking application for lottery compliance in FastField, which is a low-cost/low programming

¹ These staffing challenges have included the death of a Lottery staff member in a house fire, the retirement of the long serving liquor executive assistant/HR staff member, a key lottery employee becoming seriously ill and unable to work, and the imminent departure of the lottery’s long tenured financial manager for a position at the New York Lottery. These staff losses are made more significant by the fact that staffing levels in both division are hyper-lean with no identifiable back-up staff for some roles.

application, that has been used very successfully by Liquor for the last eighteen months. There are plans to further use Liquor staff, including investigators and minors, to assist with lottery security.

- Education and training of lottery agent staff is another area where the consolidation will be helpful. Presently, all staff that sell liquor and/or tobacco products are required to be trained and certified. Since there is significant overlap, especially at convenience stores, an effort is underway to add a component to the education program that will include lottery best practices. In fact, the education program recently received \$60,000 in grant money to help revamp our educational offerings.
- Each division has IT staff through the Agency of Digital Services (ADS). We are working with ADS to consolidate management of IT staff under the Liquor IT Director. This will allow the work of both divisions to be better allocated amongst the five existing IT staff members. More importantly, this will create bench strength at Lottery where there is a single IT staff person with very specialized knowledge and skills with no back-up in place. This creates a single-point of failure that threatens lottery operations.
- We are working to create a single licensing unit for the Department. Commonly, convenience stores sell beer, wine, tobacco and lottery products. Presently, a store owner applies for a tobacco and liquor license from Liquor and applies separately to Lottery to sell lottery products. Prior to the consolidation Liquor was working to create a more efficient on-line licensing system, and this effort is continuing. Our goal is to create a single licensing unit for all licenses issued by the Department. We will have a single licensing application and applicants will specify which licenses they would like to obtain on this single form. The end result of this change will be improved customer service for the applicant and increased efficiency for the Department as duplicative work will be eliminated.
- Each division presently has a separate financial office. With the departure of the Lottery finance manager we are reclassifying that position as a Financial Director whose role it will be to oversee financial operations of both divisions. This person will supervise the planned five-person financial staff. This will have a number of benefits including allowing the creation of a single budget for the Department and increased bench strength by combining staff from both divisions into a single unit.
- One of the challenges in the operation of very small departments is the lack of staff bench strength which, as noted above, creates potential single-points of failure. While both Liquor and Lottery maintain lean staffing levels, the twenty-person lottery staff is particularly challenged by this lack of bench strength. Fortunately, the lottery has long serving dedicated employees, with many having more than twenty years of service. The consolidation has the potential to improve this lack of staff depth as has been noted above related to IT services. To fully obtain this benefit it is necessary to have a single administrative office for the Department as soon as possible.

3. Facility Update

The legislation requires that detailed information be included in this report on the Department's progress in securing a facility that will meet the present and future office and warehouse needs of the combined entity.

For background, the Lottery offices are located on Barre-Montpelier Road in leased space which cost approximately \$13,069 per month. The lease expires in August of 2019. The space was outfitted for the Lottery in 2004 and includes 5,000 square feet of warehouse space and a customer service window. The Liquor offices are located on Green Mountain Drive in Montpelier. The space was first occupied by Liquor in 1963 and included the present office space and about 15,000 square feet of warehouse space. The warehouse was expanded in 1971 with the addition of a second building which doubled the square footage to 30,000. As you might imagine, Liquor staffing and warehouse needs have changed since 1963. Some staff in the Liquor offices work in a windowless basement "office." Others work out of cubicles in former hallways and alcoves. The education training room is in the basement and is windowless, and the Board meeting room is cramped and often overfilled for larger Board hearings. The warehouse building has deteriorated with large cracks in the brick walls and the unreinforced concrete floors which were not intended for the picking and forklift equipment now in use. The space is also very inefficient to operate as over 2000 product SKUs are stored and must be picked from ground level to 25 feet up on shelving greatly reducing order picking speed. The warehouse is also at the point of being over capacity. In December the warehouse shipped out 49,000 cases of product. Even with recent improvements to the layout and racking system this put the facility at 98% of operational capacity. Picked orders were being stored in aisles around the warehouse making them even more narrow and meaning staff had to operate picking and forklift equipment around them. This resulted in increased risk to staff and increased damage to product. The only upside of the existing Liquor facility is that it is fully depreciated and does not cost the Division very much money to rent from Buildings and General Services (BGS).

Since the consolidation we have been looking at how we could efficiently create a single office and warehouse space for the Department. We are considering a large array of options in our efforts to accomplish this goal. We have worked closely with BGS staff and have had numerous meetings and planning discussions with them. Presently, BGS staff, in consultation with Department management, are preparing an RFP for consulting services to help us narrow the many possible options and find a solution that is both efficient and cost effective. It is expected the RFP will be completed in the next 30-45 days.

Here are some of the options that are under consideration:

- Build an office and warehouse space specifically to suit the Department's needs.
 - The building could be owned by the State.
 - The building could be developed and owned by a third party and leased to the Department.
 - The building could be developed and owned by a third party with a lease to own agreement.
- Identify existing available office/warehouse space and purchase or lease this space (we have looked at several facilities).

- Find existing office space and purchase or lease it to allow office consolidation. This would *not* include the Liquor warehouse.
- Build office space to allow office consolidation. This would *not* include the Liquor warehouse.
 - The building could be owned by the State.
 - The building could be developed and owned by a third party and leased to the Department.
 - The building could be developed and owned by a third party with a lease to own agreement.
- Contract with a private company either in-state or out-of-state to operate a liquor warehouse and deliver product directly to our agents.
- Contract with a private company either in-state or out-of-state, to operate a liquor warehouse which would pick store orders and ship wrapped and palatized to our existing warehouse. Our existing warehouse would function as a cross-dock with Department staff continuing to provide deliveries to our agents.

As you can see there is a wide range of options to consider. Our goal in evaluating each option is to generate the greatest amount of revenue for the Education Fund and the General Fund in the long term. We also want to reap the benefits of the consolidation as quickly as possible, keeping in mind that some of these benefits will only be fully realized once the Department office staff is located in a single facility.

4. Recommendations for Legislative Action

An area where a legislative change would be helpful is related to criminal background checks. Background checks are part of the licensing process and required by statute. The Department has been told by the Department of Public Safety that a change or addition to statute is needed to allow DLL to conduct national criminal background checks. Our goal is to conduct these in an efficient manner that will improve the customer service we provide to applicants which is a goal noted in the licensing discussion in Section 2 above. The Department would like to work with legislative council, in conjunction with the Department of Public Safety, on crafting language that permits the DLL to conduct these criminal background checks.

We have had several internal discussions relating to additional legislative changes that may be helpful as a result of the consolidation. These ideas are still in development currently. If after further evaluation they are deemed necessary or desirable, we will bring them forward for legislative consideration.

Respectfully Submitted,



Gary Kessler, Deputy Commissioner
Department of Liquor & Lottery