House Appropriations Committee
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Written Remarks Submitted for the Record
On Behalf of the Pennsylvania Liquor Control Board

Tim Holden, Chairman, testifying with
Mike Negra, Board Member
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Chairman Saylor, Chairman Bradford, House Liquor Control Committee Chairman Pyle, Chairman Deasy and members of the House Appropriations Committee, thank you for this opportunity to review the Pennsylvania Liquor Control Board's (PLCB) business and regulatory operations during the past year and discuss our fiscal year 2021-22 budget submission and plans for the future. 2020 was a year like no other, in which we all had to learn a new normal. The COVID-19 pandemic significantly impacted both the PLCB's operations and the licensed community across Pennsylvania that we regulate.

The impact of the COVID-19 pandemic on the PLCB was most publicly visible when, by March 17, 2020, all Fine Wine & Goods Spirits stores, licensee service centers and FWGS.com temporarily ceased operations. The closure, at the direction of the Wolf Administration, was part of the initial statewide effort to mitigate the spread of COVID-19. While store operations ceased, deliveries directly from our distribution centers to high volume licensees, through the licensee delivery program, continued.

On April 1, limited e-commerce sales resumed, but as expected, the exceptional demand from customers exceeded the capacity of our e-commerce infrastructure. While we created new processes to transition 120 Fine Wine & Good Spirits stores and licensee service centers to temporarily serve as e-commerce distribution centers, the high demand forced the agency to intentionally limit access to our website to control the daily number of orders. The capacity of our e-commerce operation, which fulfilled 39,000 orders in fiscal year 2018-19, was simply not designed to handle the daily volume of transactions that occur in our brick and mortar locations. As a result of the store closures and continued significant customer demand for online purchases after the stores reopened, calendar year 2020 saw astronomical e-commerce growth as compared to the prior year. In calendar year 2019, sales through FWGS.com totaled $5.7 million from 46,464 orders consisting of 172,745 units. Average orders per day were 127. In calendar year 2020, e-commerce sales through FWGS.com totaled $33.1 million (478 percent increase) from 350,580 orders (655 percent increase) consisting of 1,597,323 units (825 percent increase). Average orders per day in 2020 were 960.

On April 20, a limited number of Fine Wine & Good Spirits stores began offering curbside service. However, the constraints of a single phone line and busy signals in our stores frustrated many customers hoping to place a curbside order. During the transition to curbside service, we learned to improve our processes to make curbside delivery more efficient and the agency integrated these improvements as more stores opened. We continue to provide curbside delivery to customers who prefer this service. The challenges we encountered during the store closures informed continual improvement efforts with regard to FWGS.com and resulted in the implementation of new phone technology in Fine Wine & Good Spirits stores.

The PLCB conducted a phased re-opening of Fine Wine & Good Spirits stores for in-person shopping beginning on May 8, as counties transitioned to the yellow COVID-19 mitigation phase as designated by the Wolf Administration. Prior to opening to the public, each store was professionally sanitized, and plexiglass was installed at registers. The agency continues to be committed to operating our stores in conformity with best practices to prevent the spread of COVID-19 as recommended by the Centers for Disease Control and Prevention and the Pennsylvania Department of Health. Store employees perform enhanced and frequent cleaning and disinfecting practices; the number of customers inside a store is limited to encourage social distancing; and customers and employees are required to wear masks. If a store employee tests positive for COVID-19, the store is temporarily closed and professionally cleaned prior to re-opening. Through February 5, 74 total stores have been temporarily closed as a result of a positive COVID-19 test. The breakdown of COVID-19 store closures by month is: 6 in August, 0 in September, 2 in October, 15 in November, 31 in December, 20 in January and 0 through February 5.

The closure of all Fine Wine & Good Spirits stores, as well as the impact of COVID-19 mitigation measures on licensees with on-premises business models, significantly impacted the PLCB's total sales. Through the first eight months of fiscal year 2019-20, year-to-date sales were up by 4.5 percent. However, ultimately, fiscal year 2019-20 sales and tax revenue totaled $2.56 billion, which represented a decrease of $110.9 million or 4.1 percent. Despite the reduction in sales, the PLCB's net income increased by 9.2 percent, to $208.7 million, which was largely attributable to a decrease in other post-employment benefits costs and pension expenses.

Overall licensee sales increased by 5 percent, but this number obscures the vastly different impact the COVID-19 pandemic had on licensees with certain business models. Sales to on-premises licensees decreased 22.9 percent. In contrast, sales to grocery, convenience and mass merchant retailers with wine expanded permits increased 117.8 percent. Sales through the licensee delivery program, which provides delivery of products directly from our warehouses to high volume licensees such as grocery and convenience stores, increased from $112.6 million to $256.9 million. Volume sold, as measured by nine-liter cases, to grocery, convenience and mass merchant retailers increased from almost 1.4 million cases in fiscal year 2018-19 to more than 3 million cases in fiscal year 2019-20. The number of wine expanded permits continued to grow in 2020, and by the end of the calendar year exceeded 1,400.

In fiscal year 2019-20, the PLCB continued its significant transfers to the General Fund and other state agencies. The PLCB contributed $694.8 million to the General Fund, which included:

- $185.1 million in cash transfers;

- $365.7 million in liquor tax; and

- $143.9 million in state sales tax.

The agency also supported other state, local and community beneficiaries, which included:

- $30.8 million to fund the operations of the Pennsylvania State Police, Bureau of Liquor Control Enforcement;

- $4.3 million in license fees returned to municipalities;

- $4.2 million to support the Department of Drug and Alcohol Programs;

- $8.8 million in local sales taxes received by Philadelphia and Allegheny Counties;

- $2.2 million in grants to promote the wine and beer industries in the Commonwealth as recommended by the Pennsylvania Wine Marketing and

Research Board and the Pennsylvania Malt and Brewed Beverage Industry Promotion Board; and

- $800,000 in alcohol education grants to support the efforts of community, law enforcement and educational organizations to reduce underage and dangerous drinking.

The PLCB contributed approximately $16.4 million to other Commonwealth agencies through interagency billing. These payments included:

- $6.3 million to the Comptroller and Payroll;
- $2.7 million to the Auditor General;
- $2.2 million for Integrated Enterprise System Services;
- $3.7 million to the Office of Administration;
- $1.1 million to the Department of General Services;
- $200,000 to the Civil Service Commission; and
- $100,000 to the Treasury Department.

The COVID-19 pandemic and resulting mitigation efforts severely impacted many licensees during 2020. In response to the challenges faced by licensees, the PLCB implemented a number of special allowances. These allowances included:

- permitting retail licensees to continue sales of beer and wine for off-premises consumption even when on-premises food sales had ceased;
- easing safekeeping requirements;
- expediting certifications for licensees through the Responsible Alcohol Management Program (a requirement for wine expanded permit holders);
- relaxing beer line cleaning requirements;

- streamlining the approval process for temporary extension of premises for outdoor seating and waiving the fee; and

- refunding event permit fees for activities that had to be cancelled as a result of the COVID-19 pandemic.

The PLCB also granted permanent authority for certain licensee activities in response to the COVID-19 pandemic. Manufacturers are allowed to use the same vehicles for the delivery of beer and other products they sell (whereas they previously had to seek specific Board approval for such activities). Distilleries may shift operations to produce hand sanitizer in accordance with federal government rules. Retail and distributor licensees are authorized to sell facemasks and hand sanitizer.

Similar to the debate between the Wolf Administration and the General Assembly about legislative and executive authority during the COVID-19 pandemic, the Board engaged in a dialogue about its authority to temporarily waive certain license fees. As a result, by 2-to-1 votes in October and November 2020, the Board decided to decline to impose most fees associated with certain license renewals or validations during 2021. The licenses included are those most affected by the COVID-19 mitigation restrictions, such as restaurant, retail dispenser, club, catering club, hotel and manufacturing licenses. The total cost of the license fee waiver is estimated at $29.5 million, which will be incurred over the current fiscal year and fiscal year 2021-22.

In fiscal year 2019-20, the PLCB held two expired restaurant license auctions. Thirty-five licenses were awarded, with bids totaling $2.8 million. Since the first auction in 2016 through December 7, 2020, 258 auction licenses have been successfully issued and $31.8 million in revenue has been recognized. At this time, given the lasting impact of COVID-19 on the economy and licensees, there are no plans to conduct a license auction in 2021.

The PLCB remained committed to its alcohol education mission in fiscal year 2019-20. Two highlights of the program remain the Know When, Know How campaign and the funding of alcohol education grants to support underage and dangerous drinking prevention efforts. First launched in January 2018, the Know When, Know How program is designed to help parents of children ages eight to 12 engage in effective conversations about underage drinking with their children. In fiscal year 2019-20, an increased television and radio placement effort further expanded the audience for this important alcohol education campaign. As noted earlier, in fiscal year 2019-20, the PLCB authorized more than $800,000 in alcohol education grants to a variety of organizations across the Commonwealth. Grants included funding for activities such as alcohol assessment surveys, social norm campaigns, enforcement patrols and peer trainings.

PLCB sales in fiscal year 2020-21 have rebounded, up 3.1 percent over the prior year through January 31. While the dynamics of the COVID-19 pandemic have complicated our traditional sales projection methods, we expect sales to grow at 10.5 percent over fiscal year 2019-20 and 6.1 percent in comparison to fiscal year 2018-19.

Throughout fiscal year 2020-21, the PLCB experienced significant product supply limitations as the result of the COVID-19 pandemic. Suppliers had difficulty maintaining sufficient stock of some products because of the pandemic's impact on worldwide supply chains. While last fiscal year through January 31 suppliers fulfilled PLCB orders at a rate of 95.8 percent, fulfillment for the current fiscal year through the end of January was 68.7 percent. The agency has engaged in an ongoing dialogue with our supplier partners about these shortages and we continue to work to prioritize Pennsylvania for deliveries when products become available.

Last fall, the PLCB transitioned to a new distribution center serving southeast Pennsylvania in partnership with a new third-party logistics provider. This new distribution center is a larger, more efficient and better-located facility enabling warehousing and transportation improvements.

The PLCB's budget request for fiscal year 2021-22 includes $671.7 million for its general operations, which supports both the business and regulatory functions of the agency. This is a $47.3 million increase from the fiscal year 2020-21 executive authorization. It is important to recognize that the agency is funded through an executive authorization to spend from revenues of the State Stores Fund and receives no money from the General Fund. The PLCB remains committed to, as it has annually since fiscal year 2017-18, transferring $185.1 million to the General Fund in fiscal year 2021-22.

A significant portion of the general operations spending increase is attributable to the replacement of the PLCB's antiquated enterprise resource planning (ERP) platform. During 2020 the PLCB embarked on a project to explore the replacement of its current highly customized, limited functionality and costly to maintain ERP system. The agency recently completed a five-month blueprint project to explore the business requirements, necessary functionality, implementation timeline and total cost of a cloud-based Oracle ERP platform. Last month, the Board unanimously voted to authorize the design and implementation of a cloud-based Oracle ERP system over the next three years. This new ERP platform will transition the PLCB's business operations from a traditionally retail-focused entity to an organization with a focus on wholesale, distribution and retail functions. Further, to constrain both design and future operational costs, the agency is committed to leveraging out-of-the-box functionality to employ industry best practices. The agency's fiscal year 2021-22 budget includes $34.7 million for the ERP project, the total cost of which is estimated to be $83.1 million.

As an agency, we recognize the importance of both transparency and accountability throughout the multi-year design and implementation of a complex project like this ERP initiative. Consequently, specific statements of work, which define certain deliverables throughout this process, will be summarized for the Board and the public at the PLCB's public meetings as they are executed against the ERP purchase contract agreement. This commitment to transparency will ensure accountability from both the PLCB executive team and our Oracle partners in delivering an ERP platform that meets the business needs of the agency and allows us to better serve our retail and wholesale customers.

E-commerce was a growth segment for the PLCB prior to the COVID-19 pandemic and the increase in customers' preference for online shopping has further solidified e-commerce as a priority for the agency. The PLCB has been engaged in a multi-year project to design a new FWGS.com website. Unfortunately, the redesign encountered unanticipated technical challenges that required us to reevaluate our approach to the e-commerce project and delayed its completion. These challenges and the decision to implement a new Oracle ERP platform has led the PLCB to engage in a two-month project to explore the possibility of transitioning certain FWGS.com functions and content management to Oracle cloud platforms while maintaining the current infrastructure for back-end integration and order management. The outcome of this project will determine whether a redesigned FWGS.com website can be launched later this year.

In conclusion, we would like to take this time to sincerely thank our retail customers and licensees for their patience and understanding throughout the past year. We recognize that the initial COVID-19 mitigation efforts prevented us from providing the level of customer service we aim to achieve every day in our retail stores, licensee service centers and online. Further, we would like to thank and acknowledge our colleagues and employees in stores and offices across the state for their efforts, flexibility and commitment over the last very challenging year. Without their commitment to developing new processes and willingness to embrace a new way to work, the PLCB could not continue to fulfill its mission as an alcohol distributor, retailer and regulator.

Thank you for the opportunity to address the committee regarding the PLCB's operations during the past year and to discuss our budget submission. We would be pleased to answer any questions from members of the committee.