FINANCIAL AUDIT

Commonwealth of Pennsylvania

Pennsylvania Liquor Control Board

State Stores Fund
Liquor License Fund

Audit Report

Harrisburg, Pennsylvania
For the years ended June 30, 2018 and 2017

November 2018

EUGENE A. DEPASQUALE • AUDITOR GENERAL •

Commonwealth of Pennsylvania
Department of the Auditor General

Eugene A. DePasquale • Auditor General

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BACKGROUND

Introduction

The Pennsylvania Liquor Control Board (PLCB) is an entity of the Commonwealth of Pennsylvania (Commonwealth) authorized by law to regulate the sale and distribution of alcoholic beverages in the Commonwealth. Included within this mandate is the authority to establish, operate and maintain Pennsylvania Fine Wine & Good Spirits stores for the sale of liquor, including wine and spirits.

The PLCB serves as the Commonwealth's responsible seller of wine and spirits, regulates Pennsylvania's beverage alcohol industry and promotes social responsibility and alcohol education, while maximizing financial returns for the benefit of all Pennsylvanians.

History and Agency Overview

With the end of Prohibition in 1933, various laws regarding alcohol regulation were passed by the Pennsylvania General Assembly, including the Liquor Control Act and the Beverage License Law. These laws created the PLCB. The statutory authority for PLCB is Act 21 of April 12, 1951, P.L. 90; as reenacted by Act 14 of June 29, 1987, P.L. 32. In conformance with the Pennsylvania Liquor Code, the PLCB regulates the manufacture, possession, sale, consumption, importation, use, storage, transportation, and delivery of wine, liquor, alcohol, and malt or brewed beverages in the Commonwealth.

On June 8, 2016, Governor Wolf signed Act 39 into law. Act 39 liquor reforms changed more than 35 sections of the Liquor Code and added a number of new sections – the most sweeping changes to liquor laws in Pennsylvania since the end of Prohibition in 1933. Among other changes, the reforms allowed for sale of wine in licensed restaurants, grocery and convenience stores; pricing flexibility; customer loyalty programs; the elimination of restrictions on Sunday store hours; the auction of expired licenses; and the shipping of wine to Pennsylvania residents for personal use and businesses. It also established a grant program for developing and promoting Pennsylvania wine and beers.

The PLCB, an independent administrative board, is comprised of three members who are appointed to staggered four-year terms by the Governor with the concurrence of two-thirds of the Senate. The Board is responsible for the management of the PLCB in the areas of directing the state-operated Fine Wine & Good Spirits stores and authorizing the licensing of establishments that manufacture, transport or sell alcohol. The PLCB also provides a comprehensive program of alcohol education aimed at promoting responsible consumption and avoidance of abuse among legal consumers, and prevention of purchase and consumption by minors. The PLCB funds the operations of the Pennsylvania State Police (PSP) Bureau of Liquor Control Enforcement, which is responsible for enforcing the liquor laws and regulations throughout the Commonwealth.

BACKGROUND (Continued)

The PLCB is primarily responsible for the accounting and reporting of the Liquor License Fund and the State Stores Fund. The Liquor License Fund is an agency fund that serves as a pass-through account for fees for hotel, restaurant, and club liquor and/or beer licenses. These fees are returned semi-annually to the municipalities in which the licenses are located, while interest earned on fund deposits is credited to the Commonwealth's General Fund (General Fund).

The State Stores Fund is an enterprise fund that serves as the general operating fund for the PLCB. This fund receives revenues from the sale of goods, primarily through Fine Wine & Good Spirits stores, and various other operating revenues including fees not credited to the Liquor License Fund. The State Stores Fund also covers the costs and expenses associated with the operation and administration of all PLCB functions as outlined and prescribed by the Pennsylvania Liquor Code.

The 18 percent liquor tax and 6 percent state sales tax collected by the PLCB are transferred monthly to the General Fund. Local sales taxes collected are remitted to Philadelphia and Allegheny County, as appropriate.

The PLCB operates over 600 Pennsylvania wine and spirits stores with gross annual sales of $2.59 billion for fiscal year 2017-2018, an increase of 2.7 percent over the previous fiscal year. As a result, the PLCB's operations generated $371.5 million in liquor tax, $146.0 million in state sales tax, and provided for $185.1 million profit and cash transfers to the General Fund. The PLCB also returned $9.4 million in local sales tax to Philadelphia and Allegheny counties. Additionally, the PLCB provided $30.5 million to fund PSP's liquor control enforcement efforts, afforded $2.5 million to support the Pennsylvania Department of Drug & Alcohol Programs, awarded $1.8 million in Pennsylvania wine and malt beverage industry grants, awarded alcohol education grants of $2.3 million and returned $4.6 million to local municipalities.

BACKGROUND (Continued)

Key Facts

- All tax moneys collected are transferred to the State Treasury. All revenues remaining, after payment of PLCB operating expenses and after required appropriations are made to other entities and Commonwealth agencies, are made available to be transferred to the State Treasury.
- The PLCB is the largest purchaser of wine and spirits in the United States, and passes significant volume purchase discounts on to PLCB customers.
- The PLCB operates over 600 stores, which are leased from private landlords.
- 100% of the required state and local sales taxes are collected by the PLCB and remitted to the General Fund.
- The state liquor tax of 18% is included in the shelf price of each item.
- The PLCB outsources warehousing services for 3 distribution centers in Pennsylvania.
- In fiscal year 2017-2018, the PLCB processed approximately 76,000 license and permit applications, including 721 for wine expanded permits to license restaurants, grocery stores, and convenience stores to sell bottles of wine to go.
- The PLCB funds grants to develop and promote Pennsylvania wines and beers through agricultural research, marketing, and education.
- The PLCB has an established formal Bureau of Alcohol Education, which provides educational material to youth, legal consumers and alcohol beverage servers.
- The PLCB funds grants to colleges and universities, communities that host these institutions, municipalities, and their organizations such as law enforcement departments and non-profit organizations to develop and/or maintain environmental management prevention strategies and other proven prevention strategies to reduce dangerous and underage drinking.

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EUGENE A. DEPASQUALE
AUDITOR GENERAL

Independent Auditor's Report

The Honorable Tom Wolf Governor Commonwealth of Pennsylvania Harrisburg, PA 17120	The Honorable Tim Holden Chairman Pennsylvania Liquor Control Board Harrisburg, PA 17124

Report on the Financial Statements

We have audited the accompanying financial statements of the Pennsylvania Liquor Control Board (PLCB) - State Stores Fund, which comprise of the Statements of Net Position as of June 30, 2018 and 2017, and the related Statements of Revenues, Expenses and Changes in Net Position and Statements of Cash Flows for the years then ended, and the related notes to the financial statements; and the PLCB - Liquor License Fund, which comprise of the Statements of Fiduciary Net Position as of June 30, 2018 and 2017, and the related Statements of Changes in Fiduciary Net Position for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the PLCB - State Stores Fund and Liquor License Fund as of June 30, 2018 and 2017, and the results of the State Stores Fund's operations and its cash flows for the fiscal year then ended, and the Liquor License Fund's changes in assets and liabilities for the fiscal year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note A, the financial statements present only the PLCB and do not purport to, and do not, present fairly the financial position of the Commonwealth of Pennsylvania as of June 30, 2018 and 2017, and the changes in its financial position and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 7-10; and the schedules of pension amounts – PLCB's schedule of contributions and PLCB's schedule of proportionate share of net pension liability, and schedules of postemployement benefits other than pensions (OPEB) amounts – PLCB's schedule of contributions and PLCB's schedule of allocated share of net OPEB liability on pages 41-44 be presented to supplement the financial statements. Such information, although not a part of the financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the financial statements, and other knowledge we obtained during our audit of the financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

The Background has not been subjected to the auditing procedures applied in the audit of the financial statements, and accordingly, we do not express an opinion or provide any assurance on it.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated November 28, 2018, on our consideration of PLCB's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering PLCB's internal control over financial reporting and compliance.

November 28, 2018

Eugene A. DePasquale
Auditor General

PLCB Management's Discussion and Analysis

Management's Responsibility for the Financial Statements

PLCB management is primarily responsible for the preparation, integrity and fair presentation of the agency's financial statements. The accompanying financial statements have been prepared in accordance with accounting principles generally accepted in the United States and, as such, include amounts based on estimates and judgments by management. The PLCB maintains a system of internal controls designed to provide reasonable assurance that its financial statements are free from material misstatement due to fraud or error.

Discussion of Basic Financial Statements

The accounts of the State Stores Fund and the Liquor License Fund are reported using the accrual basis of accounting and on a fiscal year basis, comprised of 12 calendar months.

The basic financial statements included in this audit report are the State Stores Fund Comparative Statements of Net Position as of June 30, 2018 and 2017; State Stores Fund Comparative Statements of Revenues, Expenses and Changes in Net Position for the fiscal years ended June 30, 2018 and 2017; State Stores Fund Comparative Statements of Cash Flows for the fiscal years ended June 30, 2018 and 2017; the Liquor License Fund Statements of Fiduciary Net Position as of June 30, 2018 and 2017; and the Liquor License Fund Statements of Changes in Fiduciary Net Position for the fiscal years ended June 30, 2018 and June 30, 2017.

The State Stores Fund Comparative Statement of Net Position provides information about assets and liabilities and reflects the net financial position of the State Stores Fund at the end of each fiscal year. The Comparative Statement of Revenues, Expenses and Changes in Net Position reports the operating revenue activity, expenses related to such activity and operating transfers out for each fiscal year. The Comparative Statement of Cash Flows outlines the cash inflows and outflows relating to the operations for each fiscal year. The Liquor License Fund Statement of Fiduciary Net Position provides information about assets and liabilities that reflect the position of the Liquor License Fund for each fiscal year end. The Statement of Changes in Fiduciary Net Position illustrates the net asset and net liability activity throughout the fiscal year. The basic financial statements also include Notes to Financial Statements that provide additional information that is essential to a full understanding of the data provided in the statements. These statements provide current and long-term information about the PLCB's financial position.

Although the liquor tax is incorporated into the retail price of products sold by the PLCB and is discussed herein as part of the sales analysis and transfers out, neither this tax nor the state and local sales taxes are reflected as revenue in the basic financial statements.

PLCB Management's Discussion and Analysis (Continued)

Executive Summary & Highlights

Fiscal year 2017-18 sales grew 2.7 percent over the prior year as a result of volume increases of 1.8 percent as well as price adjustments on a broad range of products. PLCB fiscal year 2017-18 net income of $158.2 million was $53.4 million, or 50.9 percent, greater than last year. The substantial increase is due mainly to the price adjustments and related gross margin improvement, higher revenues from expired license auctions, and a lower assessed contribution rate for the employer share of retiree health benefits.

The Government Accounting Standards Board (GASB) recently issued statement No. 75 which requires the PLCB to record in the State Stores Fund Comparative Statement of Net Position its entire share of the Commonwealth obligation for Other Postemployment (OPEB) benefits – also referred to as retiree health benefits. The GASB accounting rule changes also specified stricter provisions regarding the interest rate used to discount the future OPEB obligation where the liability is largely unfunded. To implement the accounting change, the PLCB's July 1, 2017 OPEB obligation was restated to $858.8 million from the previously reported balance of $107.2 million. The $751.6 million increase in the OPEB obligation was also recorded as an increase to the deficit in the State Stores Fund Comparative Statement of Net Position.

Other financial highlights include:

- Higher operating income of $185.8 million, representing an increase of $54.9 million or 41.9 percent.
- Net cash flow from operating activities of $249.1 million, up $64.2 million from the prior year, funded a $185.1 million cash transfer to the General Fund, $30.5 million to fund the Pennsylvania State Police's liquor control enforcement efforts, $2.5 million in transfers to the Department of Drug & Alcohol Programs, $1.8 million in grants to the Pennsylvania wine and malt or brewed beverage industries, and $2.9 million for the PLCB's capital expenditures.
- Year-end cash and investments increased $28.9 million to $258.3 million, due to positive net cash flow from operations.
- Total liabilities increased by $670.9 million to $1.64 billion, due primarily to implementing the change in GASB accounting rules related to post-employment benefits for retiree health care costs.
- Due to the change in GASB accounting rules for OPEB retiree health care costs, the PLCB's total net position decreased significantly to a net deficit of $1.11 billion versus a deficit of $352.5 million last year.

PLCB Management's Discussion and Analysis (Continued)

Revenues and Costs

Sales

Sales and tax revenue in fiscal year 2017-18 totaled $2.59 billion, an increase of $67.8 million or 2.7 percent over fiscal year 2016-17. Excluding liquor and sales taxes, net sales of $2.07 billion were up $53.8 million, also 2.7 percent over the prior year. By product category, sales growth was higher for spirits at 2.8 percent with wine sales growing at 2.4 percent. Overall unit sales were up 1.8 percent, with the balance of the sales increase attributable to price and product mix changes.

Fiscal year 2017-18 was the first full year of activity under broad legislative changes approved last year, that among other things, allowed for wine expanded permit holders (primarily grocery and convenience stores) to sell wine. As of June 30, 2018, almost 580 grocery and convenience retailers were selling wine to consumers. As a result, PLCB store retail wine sales decreased by 3.3 percent, while wine sold to licensees at a discount - including grocery and convenience stores - increased by 27.5 percent. Retail spirit sales increased by 3.1 percent, with spirit sales to licensees up by 1.7 percent.

Operating Income & Expense

Operating income for the fiscal year ended June 30, 2018, was $185.8 million, up $54.9 million, or 41.9 percent from the $130.9 million reported last year. The increase is partially attributable to an increase in gross profit of $36.1 million along with an increase in license fees of $15.6 million. The increase in license fees resulted from higher revenue from expired license auctions fees ($12.4 million), and higher licensee renewal surcharges ($3.8 million), partially offset by other licensee fee category decreases. Total operating expenses for the year were $522.6 million versus $525.2 million last year, a $2.6 million decrease which also lifted operating income for the year.

The reduction in operating expenses was driven primarily by a $17.4 million reduction in OPEB retiree health benefit costs due in part to a lower assessed contribution rate and to an increase in the discount rate in fiscal year 2017-18 which lowered the present value of the OPEB liability as of June 30, 2018. Operating expense was also favorably impacted by a $4.3 million decrease in IT consulting and contractual services. Pension expense declined by $1.3 million, yet still represents more than 41 percent of annual salary and wage expense. Partially offsetting these expense decreases was an increase of $4.9 million in workers compensation costs arising entirely

PLCB Management's Discussion and Analysis (Continued)

from an adjustment to the Commonwealth's workers compensation liability last year that reduced fiscal year 2016-17 expense. Salary and wages increased by $3.5 million or 2.0 percent due to Commonwealth negotiated rate increases, offset by lower overtime and staffing. Store rent increased $2.0 million or 4 percent due to premium upgrades and store re-branding efforts.

Finally, advertising expenses increased by $1.5 million for product marketing and support of alcohol education programs.

Transfers Out

The Bureau of Liquor Control Enforcement within the Pennsylvania State Police received $30.5 million in funding in fiscal year 2017-2018, an increase of $2.4 million, or 8.6 percent, over the previous year. Department of Drug & Alcohol Programs received $2.5 million, as mandated by Act 42 of 2018 and $185.1 million was transferred to the General Fund pursuant to 47 P.S. §8-802(f) and as determined annually by the Governor's Office. Grants awarded and paid to the Pennsylvania wine and malt beverage industries totaled $800,000 and $1.0 million, respectively.

Other contributions to the General Fund during fiscal year 2017-18 generated by the PLCB's operations, but not reflected as revenues, expenses, or cash flows in the State Stores Funds financial statements, included $371.5 million in liquor tax and $146.0 million in state sales tax, an overall 2.7 percent increase. Additionally, the PLCB remitted $9.4 million in local sales taxes to Philadelphia and Allegheny counties.

Licensing fees returnable to local municipalities from the Liquor License Fund were $4.6 million for fiscal year 2017-18, compared to $4.3 million in the prior year.

PENNSYLVANIA LIQUOR CONTROL BOARD

FINANCIAL STATEMENTS

PENNSYLVANIA LIQUOR CONTROL BOARD
STATE STORES FUND
COMPARATIVE STATEMENTS OF NET POSITION
(AMOUNTS IN THOUSANDS)

ASSETS	**June 30, 2018**	**June 30, 2017**
Current assets:		
Cash	$ 54,183	$ 40,011
Temporary investments	204,076	189,403
Accounts and claims receivable, net	731	2,107
Due from other funds	849	30
Merchandise inventories	257,979	254,917
Operating supplies	846	359
Prepaid expenses	73	3,083
Total current assets	$ 518,737	$ 489,910
Noncurrent assets:		
Non-depreciable capital assets – Note E:		
Land	323	323
Depreciable capital assets – Note E:		
Building	20,809	19,816
Leasehold improvements	612	583
Machinery and equipment	47,905	47,112
Intangibles	25,990	29,508
Less: accumulated depreciation	(66,663)	(61,236)
Net depreciable capital assets	$ 28,653	$ 35,783
Total noncurrent capital assets	$ 28,976	$ 36,106
Total assets	$ 547,713	$ 526,016
Total deferred outflows of resources – Note C	$ 88,631	$ 105,862
LIABILITIES		
Current liabilities:		
Trade accounts payable	$ 277,832	$ 269,949
Miscellaneous accounts payable	10,469	19,279
Accrued expenses	14,299	11,806
OPEB Note D	11,976	-
Self-insurance – Note M	7,637	6,740
Due to other funds – Note F	19,986	8,553
Due to fiduciary funds	1,932	1,906
Due to other governments	526	484
Total current liabilities	$ 344,657	$ 318,717
Noncurrent liabilities:		
OPEB – Note D	781,379	107,216
Self-Insurance – Note M	47,949	42,257
Net pension liability – Note C	440,677	477,444
Compensated absences	20,810	18,905
Total noncurrent liabilities	$ 1,290,815	$ 645,822
Total liabilities	$ 1,635,472	$ 964,539

PENNSYLVANIA LIQUOR CONTROL BOARD
STATE STORES FUND
COMPARATIVE STATEMENTS OF NET POSITION (Continued)
(AMOUNTS IN THOUSANDS)

	June 30, 2018	June 30, 2017
Total deferred inflows of resources – Note C	$ 108,179	$ 19,818
NET POSITION		
Investment in capital assets, Net of related debt	$ 28,976	$ 36,106
Deficit – Note N	(1,136,283)	(388,585)
Total net position	$ (1,107,307)	$ (352,479)

- The notes to the financial statements are an integral part of this statement. -

PENNSYLVANIA LIQUOR CONTROL BOARD
STATE STORES FUND
COMPARATIVE STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET POSITION
(AMOUNTS IN THOUSANDS)

	Fiscal Year Ended June 30, 2018	Fiscal Year Ended June 30, 2017
Sales net of taxes	$ 2,066,562	$ 2,012,789
Cost of goods sold	(1,408,532)	(1,390,882)
Gross profit from sales	$ 658,030	$ 621,907
Operating (expenses):		
Retail operations	(398,301)	(400,020)
Marketing and merchandising	(15,052)	(14,792)
Supply chain	(8,970)	(10,419)
Wholesale operations	(1,774)	(1,194)
Information technology services	(31,225)	(33,086)
Regulatory affairs	(20,803)	(22,280)
Administration	(14,782)	(14,430)
Finance	(3,891)	(3,717)
Board and secretary	(6,660)	(6,145)
Legal	(3,603)	(3,067)
Commonwealth-provided services	(14,819)	(13,437)
Total	$ (519,880)	$ (522,587)
Operating profit	$ 138,150	$ 99,320
Other operating revenues (expenses):		
Enforcement fines	1,522	1,353
License fees	46,378	30,813
Miscellaneous income	2,418	2,020
Administrative law judge	(2,709)	(2,623)
Total	$ 47,609	$ 31,563
Total operating income	$ 185,759	$ 130,883
Nonoperating revenues (expenses):		
Interest income	2,998	2,225
Other	19	(106)
Total	$ 3,017	$ 2,119
Income before operating transfers	$ 188,776	$ 133,002
Operating transfers out:		
PSP enforcement – Note J	(30,528)	(28,107)
Income after enforcement/before other transfers	$ 158,248	$ 104,895
Other operating transfers:		
Transfers out:		
General Fund – Note H	(185,100)	(216,696)
Drug and alcohol programs – Note I	(2,500)	(2,500)
Total	$ (187,600)	$ (219,196)
Change in net position	$ (29,352)	$ (114,301)
Net position – July 1, 2017 balance restated – Note N	$(1,077,955)	$ (238,178)
Total net position – ending	$(1,107,307)	$ (352,479)

- The notes to the financial statements are an integral part of this statement. -

PENNSYLVANIA LIQUOR CONTROL BOARD
STATE STORES FUND
COMPARATIVE STATEMENTS OF CASH FLOWS
(AMOUNTS IN THOUSANDS)

	Fiscal Year Ended June 30, 2018	Fiscal Year Ended June 30, 2017
Cash flows from operating activities:		
Receipts from customers	$ 2,117,437	$ 2,046,406
Payments to suppliers	(1,868,357)	(1,861,485)
Net cash provided by (used for) operating activities	$ 249,080	$ 184,921
Cash flows from noncapital financing activities:		
Operating transfers out	(220,403)	(245,856)
Net cash used for noncapital financing activities	$ (220,403)	$ (245,856)
Cash flows from capital and related financing activities:		
Acquisition and construction of capital assets	(2,862)	(7,267)
Proceeds from capital assets	33	32
Net cash used for capital and related financing activities	$ (2,829)	$ (7,235)
Cash flows from investing activities:		
Purchase of investments	(1,471,191)	(1,549,743)
Proceeds from sale and maturities of investments	1,456,517	1,635,736
Investment income	2,998	2,225
Net cash used in investing activities	$ (11,676)	$ 88,218
Net increase in cash	$ 14,172	$ 20,048
Cash – beginning of year	40,011	19,963
Cash – end of year	$ 54,183	$ 40,011
Reconciliation of operating income (loss) to net cash provided by (used for) operating activities:		
Operating income	$ 185,759	$ 130,883
Depreciation	9,978	10,239
Change in assets and liabilities:		
Accounts receivable	1,376	(626)
Inventory	(3,549)	(10,624)
Due from other funds	(819)	57
Other operating net assets	3,010	(3,083)
Deferred outflows – pension related	43,388	(12,670)
Accounts payable and accrued liabilities	1,566	11,196
Due to other funds	13,709	(1,581)
Due to pension trust funds	26	304
Net pension liability	(36,767)	28,268
Due to other governments	42	3
Deferred inflows – pension related	88,361	14,182
Other post-employment benefit obligations	(65,494)	17,038
Self-insurance liabilities	6,589	1,937
Compensated absences	1,905	(602)
Total adjustments	$ 63,321	$ 54,038
Net cash provided by (used for) operating activities	$ 249,080	$ 184,921

- The notes to the financial statements are an integral part of this statement. -

PENNSYLVANIA LIQUOR CONTROL BOARD
LIQUOR LICENSE FUND
STATEMENTS OF FIDUCIARY NET POSITION
(AMOUNTS IN THOUSANDS)

ASSETS	June 30, 2018	June 30, 2017
Current assets:		
Cash in transit	$ 89	$ 86
Investments – short term	2,508	2,390
Total assets	$ 2,597	$ 2,476

LIABILITIES	June 30, 2018	June 30, 2017
Current liabilities:		
License fees due to municipalities	$ 2,597	$ 2,476
Total liabilities	$ 2,597	$ 2,476

- The notes to the financial statements are an integral part of this statement. -

PENNSYLVANIA LIQUOR CONTROL BOARD
LIQUOR LICENSE FUND
STATEMENT OF CHANGES IN FIDUCIARY NET POSITION – Fiscal Year Ended June 30, 2018
(AMOUNTS IN THOUSANDS)

	Balance June 30, 2017	Additions	Deductions	Balance June 30, 2018
ASSETS				
Cash	$ 86	$ 8,998	$ 8,995	$ 89
Temporary investments	2,390	4,513	4,395	2,508
Total assets	$ 2,476	$ 13,511	$ 13,390	$ 2,597
LIABILITIES				
Due to municipalities	$ 2,476	$ 4,603	$ 4,482	$ 2,597
Total liabilities	$ 2,476	$ 4,603	$ 4,482	$ 2,597

- The notes to the financial statements are an integral part of this statement -

PENNSYLVANIA LIQUOR CONTROL BOARD
LIQUOR LICENSE FUND
STATEMENT OF CHANGES IN FIDUCIARY NET POSITION – Fiscal Year Ended June 30, 2017
(AMOUNTS IN THOUSANDS)

	Balance June 30, 2016	Additions	Deductions	Balance June 30, 2017
ASSETS				
Cash	$ 92	$ 8,995	$ 9,001	$ 86
Temporary investments	2,327	4,486	4,423	2,390
Total assets	$ 2,419	$ 13,481	$ 13,424	$ 2,476
LIABILITIES				
Due to municipalities	$ 2,417	$ 4,574	$ 4,515	$ 2,476
Other liabilities	2	-	2	-
Total liabilities	$ 2,419	$ 4,574	$ 4,517	$ 2,476

- The notes to the financial statements are an integral part of this statement. -

NOTE A – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The significant accounting policies employed by the Pennsylvania Liquor Control Board (PLCB) in the preparation of the accompanying financial statements are as follows:

Fund Accounting: The PLCB is primarily responsible for the accounting and reporting of the State Stores Fund and the Liquor License Fund. The State Stores Fund is an enterprise fund primarily used to account for wine and spirit sales and related operating expenses. The Liquor License Fund is an agency fund used for the collection and subsequent disbursement of certain annual license fees, which are returned to municipalities.

The preparation of financial statements in conformity with generally accepted accounting principles requires the PLCB to make estimates and assumptions that affect the reported amount of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Basis of Accounting: The State Stores Fund is reported using the economic resources measurement focus and the accrual basis of accounting. Under this measurement focus, all assets, deferred outflows of resources, liabilities, and deferred inflows of resources associated with the operations of this fund are included in the State Stores Fund Statement of Net Position. Under the accrual basis of accounting, revenues are recognized in the fiscal year earned and expenses are recognized in the fiscal year incurred. Also note, all dollar amounts in the financial statements and notes are stated in thousands unless otherwise indicated.

The Liquor License Fund, a fiduciary type fund, uses the accrual basis of accounting to report assets and liabilities. This fund has no measurement focus and does not report operating activity.

Cash: Cash includes PLCB funds held by the State Treasurer, imprest balances held at financial institutions and change used at state stores.

Temporary Investments: The PLCB participates in the Treasury Department's Commonwealth Investment Program (CIP) with other Commonwealth agencies. Practically all individual funds which are part of the Commonwealth are participants in the CIP. The Treasury Department accounts for each participating fund's equity (considered "shares") in the CIP on a daily basis. "Share" balances of participating funds fluctuate considerably during the fiscal year, based on the timing of cash receipts and disbursements in the participating fund, and are reported as temporary investments. The CIP is considered an internal investment pool. Temporary investments are reported at fair value.

LIQUOR LICENSE FUND – JUNE 30, 2018 (amounts in thousands)

NOTE A – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Cash Equivalents: No investments which could be defined as cash equivalents have been treated as such on the Statement of Cash Flows; therefore, only net changes in cash are displayed.

Inventories: Inventories are stated at weighted average cost. The PLCB utilizes a bailment inventory management program. PLCB enters into bailment agreements with certain suppliers that require the suppliers to continue to hold title to stock at PLCB warehouse facilities until it is withdrawn from bailment for shipment to PLCB stores. Product warehousing and handling, as well as transportation to store costs, are reported as part of merchandise inventories and are charged to cost of goods sold as product is sold.

The allowance for obsolete inventory was $227 at June 30, 2018 and $193 at June 30, 2017. Management will regularly review, at least once annually, inventory quantities on hand and increase/decrease the provision for obsolete inventory as necessary based upon factors that include historical unsalable product write-off, the age of the inventory and forecasts of product demand.

Capital Assets and Depreciation: Capital assets are reported at cost in the State Stores Fund Statement of Net Position. The cost of land is reported; for other types of capital assets, the following minimum per item dollar reporting thresholds are used (amounts in whole dollars):

Building	$5,000
Leasehold improvements	$5,000
Machinery and equipment	$5,000
Intangible assets	$5,000

Capital assets (excluding land) are depreciated over the useful lives using the straight-line method. The following useful lives are being used:

Building	10-20 years
Leasehold improvements	3-15 years
Machinery and equipment	5-10 years
Intangible assets	5-10 years

LIQUOR LICENSE FUND – JUNE 30, 2018 (amounts in thousands)

NOTE A – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Taxes: An 18 percent state liquor excise tax and a 6 percent state sales tax are collected and remitted monthly to the Department of Revenue for the General Fund. The PLCB also collects and remits a 1 percent local sales tax for Allegheny County and a 2 percent local sales tax for Philadelphia County. Taxes collected for the fiscal years ended June 30, 2018 and June 30, 2017 are as follows:

	Fiscal Year Ended June 30, 2018	Fiscal Year Ended June 30, 2017
Liquor Tax	$371,508	$361,856
State Sales Tax	146,027	142,005
Local Sales Tax	9,398	9,060
Total	$526,933	$512,921

Sales are reported net of these collected and remitted taxes in the financial statements.

Compensated Absences: From July 1, 2016 to the end of the 2016 leave calendar year, employees accumulated annual leave based on 2.7 to 10 percent of regular hours paid. Effective with the beginning of the 2017 leave calendar year, employees accumulate annual leave based on 4.24 to 11.93 percent of regular hours paid. Generally, a maximum of 45 days may be carried forward at the end of each leave calendar year. Employees are paid for accumulated annual leave upon termination or retirement.

Employees earn sick leave based on an agreed upon percentage of regular hours paid. Generally, a maximum of 300 days may be carried forward at the end of each leave calendar year. Most retiring employees that meet service, age or disability requirements are paid in accordance with the following schedule:

Days Available at Retirement	Percentage Payment	Maximum Days Paid
0-100	30%	30
101-200	40%	80
201-300	50%	150
Over 300 (in last year of employment)	100% of days over 300	11

The accumulated annual and sick leave and related payroll benefits payable reported for the fiscal years ended June 30, 2018 and June 30, 2017 was $25,691 ($4,881 current and $20,810 non-current) and $24,552 ($5,647 current and $18,905 non-current), respectively. It is the PLCB's

LIQUOR LICENSE FUND – JUNE 30, 2018 (amounts in thousands)

NOTE A – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

policy to record the cost of annual and sick leave in accordance with Governmental Accounting Standards Board (GASB) Statement No. 16. The expense and corresponding liability are reflected in the financial statements.

The following summary provides aggregated information reported for the fiscal years ended June 30, 2018 and June 30, 2017 of the compensated absences liabilities to include the additions and reductions during the fiscal years then ended:

Fiscal Year End	Liability – Beginning Balance	Additions	Reductions	Liability – Ending Balance
June 30, 2018	$24,552	$17,731	$16,592	$25,691
June 30, 2017	$24,384	$17,455	$17,287	$24,552

Pension Costs and Liability: The PLCB participates in the State Employees' Retirement System (SERS) cost-sharing, multiple-employer defined-benefit pension plan. The Commonwealth's policy is to fund employer contributions to the SERS as required by the SERS Board, through statutory authority, or as required based on other applicable statutory requirements. As prescribed by GASB Statement No. 68, an actuarial valuation was prepared to value the SERS pension liability, deferred outflows of resources, and deferred inflows of resources at the actuarial present value of projected benefit payments related to periods of employee service.

In the State Stores Fund Statement of Net Position, the PLCB reports its share of the net pension liability, deferred outflow of resources, and deferred inflow of resources. The changes in the net pension liability will be recognized in pension expense. Balances projected for the deferred outflow of resources and deferred inflow of resources will be amortized over a closed period matching the expected remaining service life of all employees or a closed period of five years.

Other Postemployment Benefit (OPEB) Costs and Liability: The PLCB participates in the Commonwealth's single employer defined benefit OPEB plan, the Retired Employees Health Program (REHP). The Commonwealth's policy is to fund employer contributions to the REHP under contribution policies established by the Office of Administration and the Office of the Budget. As prescribed by GASB Statement No. 75, an actuarial valuation was prepared to value the OPEB liability, deferred outflow of resources, and deferred inflow of resources for the REHP at the actuarial present value of projected benefit payments related to periods of employee service.

NOTE A – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

In the State Stores Fund statement of net position, the PLCB reports its share of the net OPEB liability, deferred outflow of resources, and deferred inflow of resources. The changes in the net OPEB liability will be recognized in OPEB expense. Balances projected for the deferred outflow of resources and deferred inflow of resources will be amortized over a closed period matching the expected remaining service life of all employees or a closed period of five years.

New accounting Pronouncements – Adopted:
The PLCB adopted GASB Statement No. 75, "Accounting and Financial Reporting for Postemployment Benefits other Than Pensions" for the fiscal year ended June 30, 2018, which superseded GASB Statement No. 45. See Note D for OPEB related disclosures and Note N for restatement information. The fiscal year ended June 30, 2017 is still reported under GASB Statement No. 45 due to the GASB Statement No. 75 required actuarial information not being available for the period.

New accounting Pronouncements – To Be Adopted:
GASB issued Statement No. 84, "Fiduciary Activities" in January 2017. The objective of this statement is to improve the guidance regarding the identification of fiduciary activities for accounting and financial reporting purposes and how those activities should be reported. This statement will be effective for the PLCB's financial statements for fiscal year ended June 30, 2020.

GASB issued Statement No. 87, "Leases" in June 2017. This Statement establishes a single model for lease accounting based on the principle that leases are financings of the right to use an underlying asset. Under this statement, a lessee is required to recognize a lease liability and an intangible right-to-use lease asset, and a lessor is required to recognize a lease receivable and deferred inflow of resources. The PLCB currently leases over 600 store properties for their retail operations, and this statement will be effective for the PLCB's financial statements for the fiscal year ended June 30, 2021.

NOTE B – DEPOSITS AND INVESTMENTS

The Treasury Department has the authority to manage, invest, and reinvest the moneys of all funds which are not legally authorized to be invested by a board, commission or State officer. The Treasury Department manages and invests moneys of the Commonwealth through the Commonwealth Investment Program (CIP). The PLCB participates in the CIP's Pool 999 investment pool. Pool 999 is designed to provide a high degree of liquidity and safety. Pool 999 is organized similarly to a money market fund, with an expectation of a stable net asset value per share. Treasury accounts for each participating fund's equity, or shares, in the pool on a daily

NOTE B – DEPOSITS AND INVESTMENTS (Continued)

basis. Share balances of participating funds vary considerably during the fiscal year, based on the timing of cash receipts and disbursements. PLCB has reported the fair value of its shares as of June 30, 2018 and 2017, the fund's year-end. Shares in Pool 999 are reported as temporary investments.

The CIP pools are considered internal investment pools of the Commonwealth of PA and are subject to the requirements of GASB Statement No. 40. GASB Statement No. 40 requires state and local governments to make certain disclosures relating to investment risk, consisting of credit risk (including custodial credit risk and concentrations of credit risk), interest rate risk, and foreign currency risk, in addition to custodial credit risk and foreign currency risk on deposits. The Treasury Department has formally adopted written investment policies to address these investment risks and has disclosed those risks associated with its total pooled deposits and investments in the Commonwealth of Pennsylvania's June 30, 2018 Basic Financial Statements.

PLCB's total deposit balance of $54,273 and $40,098 at June 30, 2018 and 2017, respectively, was not exposed to either custodial credit risk or foreign currency risk.

As a participant in Treasury's CIP Pool 999, PLCB's investments are exposed to credit risk and interest rate risk mentioned above. Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The credit risk of fixed income instruments susceptible to credit quality rating is measured by nationally recognized statistical rating agencies (or NRSRAs) such as Moody's Investors Service. Treasury's CIP investment pools are not rated by an NRSRA. Interest rate risk is the risk that an investment's value will change, advantageously or adversely, due to a change in the absolute value of interest rates. The Treasury Department measures interest rate risk using option adjusted duration. Duration is a measure of an investment's sensitivity to changes in interest rates. The higher the duration, the greater the changes in fair value when interest rates change. The average option adjusted duration of Treasury's CIP Pool 999 at June 30, 2018 is approximately 0.083 years.

NOTE C – PENSION

General Information about the Pension Plan

Plan Description: To provide pension benefits for employees of state government and certain other organizations, the SERS administers a cost-sharing multiple-employer defined benefit retirement plan. The plan, covering substantially all Commonwealth employees, is a contributory defined benefit pension plan as established by Commonwealth laws. Membership in the SERS is mandatory for most PLCB (and other state) employees. Article II of the Commonwealth's constitution assigns the authority to establish and amend the benefit provision of the plan to the General Assembly.

NOTE C – PENSION (Continued)

The SERS issues stand-alone, audited financial statements which are publicly available at www.sers.pa.gov. Written requests for financial statements should be directed to the following address:

State Employees' Retirement System
30 North Third Street, Suite 150
Harrisburg, PA 17101-1716

Benefits Provided: Under the plan, for most employees hired prior to January 1, 2011, retirement benefits vest after 5 years of credited service. Generally, employees who retire at age 60 or, if under age 60, with 35 years of service are entitled to a normal (unreduced) annual retirement benefit. The general annual benefit is 2 percent of a Class A member's highest three-year average salary multiplied by years of service. This annual benefit is 2.5 percent for Class AA members.

Act 120 of 2010 (Act 120), which preserved all benefits in place for then current members, mandated a number of benefit reductions for new members effective January 1, 2011. The benefit reduction included a new class of membership that accrues benefits at 2 percent of their final average salary instead of the previous 2.5 percent. The new vesting period changed from 5 to 10 years of credited service, and the option to withdraw lump sum accumulated employee contributions was eliminated. The new normal retirement age is 65 for most employees. Act 120 created a new A-3 class of service and an optional A-4 class for most employees that entered SERS membership for the first time on or after January 1, 2011. The general annual benefit for Class A-3 members is 2 percent of the member's highest three-year average salary times years of service while the Class A-4 benefit accrual rate is 2.5 percent.

Contributions: Section 5507 of the State Employees Retirement Code (SERC) (71 Pa. C.S. §5507) requires the Commonwealth and other employers whose employees are the SERS members to make contributions to the fund on behalf of all active members and annuitants necessary to fund the liabilities and provide the annuity reserves required to pay benefits. The SERS funding policy, as set by the SERS board, provides for periodic active member contributions at statutory rates. The SERS funding policy also provides for periodic employer contributions at actuarially determined rates based on the SERS funding valuation, expressed as a percentage of annual covered payroll, such that they, along with employee contributions and an actuarially determined rate of investment return, are adequate to accumulate assets to pay benefits when due. However, Act 120 imposed rate increase collars (limits on annual rate increases) on employer contributions. The collar for Commonwealth fiscal year 2016-17 was 4.5%. For fiscal year 2017-18 the actuarial determined contribution rate increase over the prior year was within the legislative collar of 4.5%, so the collar was not in effect. The PLCB's contributions to the SERS were $52,427 and $45,199 for the fiscal years ended June 30, 2018 and 2017, respectively.

LIQUOR LICENSE FUND – JUNE 30, 2018 (amounts in thousands)

NOTE C – PENSION (Continued)

Summary of Significant Accounting Policies: The SERS financial statements are prepared on the accrual basis of accounting, whereby expenses are recorded when the liability is incurred, revenues are recorded in the accounting period in which they are earned and become measurable, and investment purchases and sales are recorded as of the related trade date. Member and employer contributions are recognized in the period in which employee salaries are reported. Benefits and refunds are recognized when due and payable in accordance with the terms of the plan.

Pension Liabilities, Pension Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions: The PLCB reported a liability of $440,677 and $477,444 for its proportionate share of the SERS net pension liability as of June 30, 2018 and June 30, 2017 respectively. The net pension liability attributed to participation in the SERS was measured as of December 31, 2017, and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of that date.

PLCB's proportion of the SERS net pension liability was based on a projection of the Commonwealth's long-term share of contributions to the pension plan relative to the projected contributions of all participating SERS employers, actuarially determined. At December 31, 2017, PLCB's reported proportionate share of the SERS net pension liability was 2.55 percent which was an increase of .07 percent from its proportion measured as of December 31, 2016.

For the fiscal years ended June 30, 2018 and June 30, 2017, PLCB recognized pension expense of $72,928 and $74,979, respectively, and reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

Fiscal year ended June 30, 2018

	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual experience……………………..	$ 7,451	$ 8,367
Change in assumptions..	22,063	-
Differences between projected and actual investment earnings…………...	-	17,521
Change in proportion………………………………………………………	7,384	8,664
Differences between employer contributions and proportionate share…....	974	679
Contributions subsequent to measurement date……………………………	26,136	-
Total	$ 64,008	$ 35,231

LIQUOR LICENSE FUND – JUNE 30, 2018 (amounts in thousands)

NOTE C – PENSION (Continued)

Fiscal year ended June 30, 2017

	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual experience	$ 6,893	$ 10,683
Change in assumptions	29,163	-
Differences between projected and actual investment earnings	40,124	-
Change in proportion	6,597	8,508
Differences between employer contributions and proportionate share	917	627
Contributions subsequent to measurement date	22,168	-
Total	$ 105,862	$ 19,818

For the fiscal year ended June 30, 2018, the $26,136 reported as deferred outflows of resources related to pensions resulting from PLCB's contributions to SERS subsequent to the measurement date will be recognized as a reduction of the net pension liability in the year ended June 30, 2019. Other amounts reported as deferred outflows of resources and deferred inflows of resources related to pensions will be recognized in pension expense as follows:

Year Ending June 30:	Pension Expense
2019	$ 10,592
2020	7,781
2021	(6,034)
2022	(9,863)
2023	165

Actuarial Assumptions: Every five years, SERS is required to conduct an actuarial experience study to determine whether the assumptions used in its annual actuarial valuations remain accurate based on current and anticipated demographic trends and economic conditions. The *18th Investigation of Actuarial Experience* study for the period 2011 – 2015 was released in March 2016. The actuary, under oversight of the SERS Board, reviewed economic assumptions (such as the assumed future investment returns and salary increases) as well as demographic assumptions (such as employee turnover, retirement, disability, and death rates). Some assumption adjustments increased projected cost and some decreased projected cost, but the overall result was a slight increase to the net pension liability in 2015 upon adoption.

The board adopted the actuarial assumptions set forth in the 18th Investigation of Actuarial Experience at its March 2016 meeting. The study can be viewed at www.SERS.pa.gov.

LIQUOR LICENSE FUND – JUNE 30, 2018 (amounts in thousands)

NOTE C – PENSION (Continued)

In addition to the five-year experience study, SERS reviews its investment return assumption in light of economic conditions every year as part of its annual valuation. Based on this work, SERS actuary recommended, and SERS Board adopted at the April 2017 meeting, a reduction in the targeted investment return rate assumption to 7.25 percent for the 2016 actuarial valuation from 7.5 percent used for the 2015 actuarial valuation based on the experience study. In addition, SERS actuary recommended, and SERS Board adopted, a reduction in the inflation rate to 2.6 percent for the 2016 valuation from 2.75 percent used for the 2015 actuarial valuation based on the experience study. The change in inflation rate also impacted the general salary growth rate, which was lowered to 2.9 percent for the 2016 valuation from 3.05 percent used for the 2015 valuation based on the experience study.

The following methods and assumptions were used in the actuarial valuation for the December 31, 2017, measurement date:

Actuarial Cost Method	Entry age
Amortization Method	Straight-line amortization of investments over five years and amortization of assumption changes and noninvestment gains/losses over the average expected remaining service lives of all employees that are provided benefits
Investment rate of return	7.25% net of expenses including inflation
Projected salary increases	Average of 5.60% with range of 3.70% to 8.90% including inflation
Asset valuation method	Fair (market) value
Inflation	2.60%
Mortality Rate	Projected RP-2000 Mortality Tables adjusted for actual plan experience and future improvement
Cost of living adjustments	Ad hoc

LIQUOR LICENSE FUND – JUNE 30, 2018 (amounts in thousands)

NOTE C – PENSION (Continued)

The long-term expected rate of return on pension plan investments was determined using a building-block method in which best estimate ranges of expected future real rates of return are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. The target allocation and best estimates of arithmetic real rates of return for each major asset class are summarized in the following table:

Asset Class	Target Allocation	Long-term Expected Rate of Return
Private Equity	16.00%	8.00%
Global Public Equity	43.00%	5.30%
Real Estate	12.00%	5.44%
Multi-Strategy	12.00%	5.10%
Fixed Income	14.00%	1.63%
Cash	3.00%	-0.25%
Total	100.00%	

Discount Rate: The SERS discount rate used to measure the total pension liability was 7.25 percent. The projection of cash flows used to determine the discount rate assumed that employee contributions will be made at the rates applicable for each member and that employer contributions will be made based on rates determined by the actuary. Based on those assumptions, the SERS fiduciary net position was projected to be available to make all projected future benefit payments of current active and non-active SERS members. Therefore, the long-term expected rate of return on SERS investments was applied to all periods of projected benefit payments to determine the total pension liability.

Sensitivity of the PLCB's proportionate share of the net pension liability to change in the discount rate: The following table presents the PLCB's proportionate share of the SERS net pension liability using the discount rate of 7.25 percent, as well as what the PLCB's proportionate share of the net pension liability would be if it were calculated using a discount rate that is 1 percentage point lower (6.25 percent) or 1 percentage point higher (8.25 percent) higher than the current rate.

LIQUOR LICENSE FUND – JUNE 30, 2018 (amounts in thousands)

NOTE C – PENSION (Continued)

	1% Decrease 6.25%	Current discount rate 7.25%	1% Increase 8.25%
PLCB's proportionate share of SERS net pension liability as of the 12/31/17 measurement date	$559,357	$440,677	$339,015

Pension plan fiduciary net position: Detailed information about the pension plan's fiduciary net position is available in the separately issued SERS financial report.

Payables to the pension plan: For the fiscal year ended June 30, 2018, the PLCB reported an accounts payable for the employers' share of retirement contributions to the SERS in the amount of $1,909.

Additional pertinent information regarding SERS, outside the scope of PLCB reporting, is published each year as part of the Commonwealth of Pennsylvania's Basic Financial Statements included in its Comprehensive Annual Financial Report.

NOTE D – OTHER POSTEMPLOYMENT BENEFITS

GASB Statement No. 75 Reporting for the fiscal year ended June 30, 2018:

General Information about the Pension Plan

Plan Description: The Commonwealth established and sponsors a Retired Employees Health Program (REHP) plan which provides postemployment benefits other than pensions (OPEB). This plan is administered by the Pennsylvania Employee Benefits Trust Fund, which acts as a third-party administrator and administers the REHP under an administrative agreement with the Commonwealth. The plan is a single employer defined benefit OPEB plan. The PLCB participates in the REHP, which provides a variety of healthcare benefits to eligible retirees. The REHP is provided as a part of collective bargaining agreements with most Commonwealth labor unions. All policy decisions and types and levels of benefits for the REHP fall under the purview of the Commonwealth's Executive Board and Secretary of Administration. REHP does not have a governing board. The REHP plan does not issue a stand-alone financial report nor is it included in the financial statements of a public employee retirement system.

NOTE D – OTHER POSTEMPLOYMENT BENEFITS (continued)

Benefits Provided: Benefit provisions included in the REHP plans are established and may be amended by the establishing sponsor. The REHP plan provides postemployment healthcare benefits to eligible employees. Employees who retire from the Commonwealth and meet one of the following eligibility criteria are eligible to receive REHP benefits:

- 25 or more years of service;
- 20 or more years of service and superannuation age – age 50 for Park Rangers, Capitol Police and certain enforcement officers or age 60 for all other employees (age 55 or 65 for employees subject to Act 120 of 2010);
- Disability retirement – requires five years of service (no service requirements for enforcement officers).

Contributions: REHP contribution requirements are contractually required and established by the Office of Administration and the Office of the Budget. The contributions rates are established as a set amount per current active REHP eligible employee per biweekly pay in order to fund the REHP plan. During the fiscal year ended June 30, 2018, the contractually required contribution rate for the PLCB began the fiscal year at $350 (whole dollars), was lowered to $300 after the first pay period, and then subsequently lowered again to $188 starting in January 2018. During the fiscal year ended June 30, 2017, the contractually required contribution rate for the PLCB was $362 for the entire year. For employees who retired after June 30, 2005 and before July 1, 2007 the retiree contribution is set at 1% of employee's final annual salary. PLCB employees who retired on or after July 1, 2007 but before July 1, 2011 are currently required to pay retiree contributions of 3% of either their final annual salary or final average salary, whichever is less. PLCB employees who retire on or after July 1, 2011 are currently required to pay retiree contributions of 3% of their final average salary. Upon enrollment in Medicare, PLCB employees who are currently paying 3% will pay retiree contributions of 1.5% of either their final annual salary or final average salary, whichever applies.

The REHP funding rate needed to fund current year annuitant health care costs are established as part of the Commonwealth's annual budgeting process. During the fiscal years ended June 30, 2018 and June 30, 2017, the Commonwealth funded $541,795 (estimated) and $603,720 (estimated) of annuitant health care claims and administrative costs for the REHP, respectively. Any additional contributions to advance fund annuitant health care liabilities are determined annually by the Commonwealth. During the fiscal year ended June 30, 2018, advance funding of $50,000 for REHP was contributed to the Other Postemployment Benefits Investment Pool, a pension (and other employee benefit) trust fund. The PLCB's contributions to the REHP trust for the fiscal year ended June 30, 2018 was $26,157.

LIQUOR LICENSE FUND – JUNE 30, 2018 (amounts in thousands)

NOTE D – OTHER POSTEMPLOYMENT BENEFITS (continued)

OPEB Liabilities, OPEB Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to OPEB:

At fiscal year end June 30, 2018, the PLCB reported a liability of $793,355 for its allocated share of the REHP's net OPEB liability. The net OPEB liability for the REHP was measured as of June 30, 2017, and the total OPEB liability used to calculate the net OPEB liability was determined by an actuarial valuation as of that date. The PLCB's allocation of the net OPEB liability was based on PLCB contributions to the plan relative to the total contributions to the plan over the measurement period. At June 30, 2017, the PLCB's allocation was 3.96%.

For the fiscal year ended June 30, 2018, the PLCB recognized OPEB expense of $29,068, and reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

Fiscal year end June 30, 2018:

	Deferred Outflows of Resources	Deferred Inflows of Resources
Change in assumptions..	$ -	$ 72,285
Differences between projected and actual investment earnings…………...	-	663
Contributions subsequent to measurement date……………………………	24,623	-
Total	$ 24,623	$ 72,948

The deferred outflow of contributions subsequent to measurement date of $24,623 will be recognized as a reduction of the net OPEB liability in the fiscal year ended June 30, 2019. Other amounts reported as deferred outflows and deferred inflows of resources will be recognized in OPEB expense as follows:

Year Ending June 30:	OPEB Expense
2019	$ 15,513
2020	15,513
2021	15,513
2022	15,513
2023	10,896

LIQUOR LICENSE FUND – JUNE 30, 2018 (amounts in thousands)

NOTE D – OTHER POSTEMPLOYMENT BENEFITS (continued)

Actuarial Assumptions: The total OPEB liability in the June 30, 2017 actuarial valuation was determined using the following actuarial assumptions applied to all periods included in the measurement, unless otherwise specified:

Inflation	2.60%
Salary increases	2.90%
Investment rate of return	5.00%
Healthcare cost trend rate	6.00% decreasing to an ultimate rate of 3.90%
Asset valuation method	Fair (market) value
Actuarial Cost Method	Entry age
Amortization Method	Straight-line amortization of investments over five years and amortization of assumption changes and noninvestment gains/losses over the average expected remaining service lives of all employees that are provided benefits.

Mortality rates were based on the RP-2000 Male and Female Combined Health Mortality Tables projected (using Projection Scale AA) to 2016 for males and to 2020 for females, and then further adjusted to ensure sufficient margin improvement in certain age ranges. Disabled participants mortality rates were based on the RP-2000 Male and Female Disabled Retiree Mortality Tables projected (using Projection Scale AA) to 2021 for males and to 2017 for females. Each table includes a margin for future improvement in life expectancy.

The actuarial assumptions used in the June 30, 2017 valuation were based on the State Employees' Retirement System (SERS) experience study that covered the years 2011 through 2015. The approved recommendations from that study were used to determine the assumptions for this valuation, where applicable. The inflation assumption was selected by the SERS Board during an April 2017 meeting based on a review of actual plan experience and the prevalent economic outlook. Consistent with prior valuations, these demographic assumptions assume beginning of year decrements (retirement, withdrawal, death, disability, etc.). Cost of living adjustments (COLA) may be granted on an ad hoc basis; there were no COLAs granted during the measurement period.

LIQUOR LICENSE FUND – JUNE 30, 2018 (amounts in thousands)

NOTE D – OTHER POSTEMPLOYMENT BENEFITS (continued)

The long-term expected rate of return on OPEB plan investments is determined using a risk premium review. This review compares the current relationship between fixed income and equity and their relationship over long periods of time to come up with an expected rate of return. Other variables considered in the expected rates of return are a reversion to the mean for each asset class. Best estimates of arithmetic real rates of return for each major asset class included in the target asset allocation as of June 30, 2017 are summarized in the following table:

Asset Class	Target Allocation	Long-term Expected Rate of Return
Domestic Equity	47.00%	7.50%
International Equity	20.00%	8.50%
Fixed Income	25.00%	3.00%
Real Estate	8.00%	7.50%
Cash and Cash Equivalents	0.00%	1.00%
Total	100.00%	

Discount Rate: The discount rate used for the total OPEB liability reported at June 30, 2018 was 3.58%. This single discount rate was based on the 20-year Bond Buyer GO Index municipal bond rate as of the measurement date of June 30, 2017. Since REHP has insufficient assets to meet next year's projected benefit payments, the municipal bond rate was applied to all periods of the projected benefit payments to determine the total OPEB liability. The projection of cash flows used to determine the single discount rate for each fiscal year end assumed that employer contributions will be made based on the current funding policy for future years.

The discount rate used in the restatement of the net OPEB liability as of July 1, 2017 was 2.85% based on the 20-year Bond Buyer GO Index municipal bond rate as of June 30, 2016. The increase in discount rate resulted in a gain that decreased the net OPEB liability by $87,632, of which $15,347 was recognized as a reduction to expense in the current period and $72,285 was reported as a change in assumption deferred inflow.

Sensitivity of the net OPEB liability to changes in the discount rate: The following presents the net OPEB liability of the PLCB, as well as what the PLCB's net OPEB liability would be if it were calculated using discount rate that are one percentage point lower (2.58 percent) or one percentage point higher (4.58 percent) than the current healthcare cost trend rates.

LIQUOR LICENSE FUND – JUNE 30, 2018 (amounts in thousands)

NOTE D – OTHER POSTEMPLOYMENT BENEFITS (continued)

	1% Decrease 2.58%	Current discount rate 3.58%	1% Increase 4.58%
PLCB's proportionate share of REHP net OPEB liability as of the 6/30/2017 measurement date	$ 929,554	$ 793,355	$ 703,020

Sensitivity of the net OPEB liability to changes in the healthcare cost trend rates: The following presents the net OPEB liability of the PLCB, as well as what the PLCB's net OPEB liability would be if it were calculated using healthcare cost trend rates that are one percentage point lower (5.0% decreasing to 2.9%) or one percentage point higher (7.0% decreasing to 4.9%) than the current healthcare cost trend rates.

	1% Decrease 5% grading down to 2.9%	Current health trend rate 6% grading down to 3.9%	1% Increase 7% grading down to 4.9%
PLCB's proportionate share of REHP net OPEB liability as of the 6/30/2017 measurement date	$ 688,508	$ 793,355	$ 950,308

OPEB plan fiduciary net position: Detailed information about the REHP OPEB plan's fiduciary net position is available in the separately issued Commonwealth of Pennsylvania's Comprehensive Annual Financial Report (CAFR).

GASB Statement No. 45 Reporting for the fiscal year ended June 30, 2017:

During the fiscal year ended June 30, 2017, the PLCB contributed $362 (whole dollars) for each active employee paid and reported as part of biweekly payroll expenses for its employees. For the fiscal year ended June 30, 2017, the PLCB's allocated share of the total REHP Annual OPEB Cost of $1,107,290 (for the Commonwealth's fiscal year ended June 30, 2017) was $44,182. The last year that was fully funded for the entire REHP Annual OPEB Cost, for all REHP-participating organizations, was for the fiscal year ended June 30, 2008. The unfunded OPEB liability has been recorded for subsequent fiscal years. The prior year unfunded liability of $90,178, plus an additional increase of $17,038, resulted in a total unfunded liability of $107,216 as of fiscal year ended June 30, 2017.

LIQUOR LICENSE FUND – JUNE 30, 2018 (amounts in thousands)

NOTE E – CAPITAL ASSETS

Changes in capital assets for the fiscal year ended June 30, 2018 are as follows:

Fiscal year ended June 30, 2018:

	Balance June 30, 2017	Additions	Retirements	Balance June 30, 2018
Non-depreciable capital assets:				
Land…………………………..	$ 323	$ -	$ -	$ 323
Depreciable capital assets:				
Building………………………..	19,816	993		20,809
Leasehold improvements……...	583	29		612
Machinery and equipment….…	47,112	1,240	447	47,905
Intangibles ……………………	29,508	599	4,117	25,990
Total capital assets…………….	$ 97,342	$ 2,861	$ 4,564	$ 95,639

Changes in capital assets accumulated depreciation for the fiscal year ended June 30, 2018 are as follows:

	Balance June 30, 2017	Additions	Retirements	Balance June 30, 2018
Buildings……………………	$ 14,100	$ 803	$ -	$ 14,903
Leasehold improvements…...	374	66	-	440
Machinery and equipment….	31,451	4,691	432	35,710
Intangibles……….………….	15,311	4,416	4,117	15,610
Total accumulated depreciation	$ 61,236	$ 9,976	$ 4,549	$ 66,663

Changes in capital assets for the fiscal year ended June 30, 2017 are as follows:

Fiscal year ended June 30, 2017:

	Balance June 30, 2016	Additions	Retirements	Balance June 30, 2017
Non-depreciable capital assets:				
Land…………………………..	$ 323	$ -	$ -	$ 323
Depreciable capital assets:				
Building………………………..	19,558	258	-	19,816
Leasehold improvements……...	758	123	298	583
Machinery and equipment….…	51,585	(3,380)	1,093	47,112
Intangibles ……………………	20,559	10,266	1,317	29,508
Total capital assets…………….	$ 92,783	$ 7,267	$ 2,708	$ 97,342

LIQUOR LICENSE FUND – JUNE 30, 2018 (amounts in thousands)

NOTE E – CAPITAL ASSETS (Continued)

Changes in capital assets accumulated depreciation for the fiscal year ended June 30, 2017 are as follows:

	Balance June 30, 2016	Additions	Retirements	Balance June 30, 2017
Buildings……………………	$ 13,311	$ 789	$ -	$ 14,100
Leasehold improvements…...	612	60	298	374
Machinery and equipment….	26,278	4,774	(399)	31,451
Intangibles…………………	13,364	4,616	2,669	15,311
Total accumulated depreciation	$ 53,565	$ 10,239	$ 2,568	$ 61,236

Negative amounts in the above additions and retirements result from reclassifications between Machinery and equipment and do not impact the overall totals.

NOTE F – DUE TO OTHER FUNDS

At June 30, 2018 and June 30, 2017, a total of $19,986 and $8,553 respectively, was due to other funds. This total was due to various funds.

NOTE G – LEASE COMMITMENTS

The PLCB, through the Department of General Services, has operating leases covering all of its Fine Wine and Good Spirits store locations and some equipment. The leases generally provide for an initial term of three to ten years. Most leases have options for renewal. For leases not renewed, but not terminated, the lease will continue as a renewal in 90-day increments into the future. For such leases, only 90 days of future rental commitments are included in the rental commitment schedule below.

Rental expenses for the fiscal years ended June 30, 2018 and June 30, 2017 were $53,346 and $51,342, respectively.

LIQUOR LICENSE FUND – JUNE 30, 2018 (amounts in thousands)

NOTE G – LEASE COMMITMENTS (Continued)

The following is a schedule of future minimum rental commitments for noncancelable operating leases in effect as of the fiscal year end June 30, 2018:

Fiscal Year Ended June	Fine Wine and Good Spirits Store Leases
2019	$54,141
2020	48,392
2021	41,568
2022	36,706
2023	32,294
Total Minimum Lease Payments:	$213,101

NOTE H – OPERATING TRANSFERS TO GENERAL FUND

The PLCB is subject to profit transfer requirements pursuant to 47 P.S. §8-802(f), determined annually by the Governor's Office, whereby stipulated funds are transferred to help finance the General Fund.

Per Act 39 of 2016, any commissions, compensation or any type of incentive award based upon the sale of lottery tickets and games shall be deposited by the PLCB into the General Fund.

Per Act 166 of 2016, all moneys collected from converting an eating place retail dispensing license to a restaurant license, casino license fees, and license auction proceeds shall be transferred from the State Stores Fund to the General Fund.

The required transfers to the General Fund totaled $185,100 and $216,700 for the fiscal years ended June 30, 2018 and June 30, 2017, respectively.

NOTE I – OPERATING TRANSFER AND LIABILITIES FOR DRUG AND ALCOHOL PROGRAMS

Per Act 14 of 1987, two percent of the PLCB's profits from the sale of alcohol shall be transferred to the Department of Drug & Alcohol Programs (DDAP) for drug and alcohol rehabilitation programs. The PLCB establishes a liability for the amount due to the DDAP and transfers the payment in the subsequent fiscal year. Act 44 of 2017 and Act 42 of 2018 have since superseded the two percent requirements mandated by Act 114 of 1987.

Act 44 of 2017 was enacted on October 30, 2017 and contained a provision that resulted in a $2,500 other operating transfer to DDAP for fiscal year 2016-2017 (for fiscal year 2017-2018 transfer) for the purposes set forth in Act 14 of 1987.

Act 42 of 2018 was enacted on June 22, 2018 and contained a provision that resulted in a $2,500 other operating transfer to DDAP for fiscal year 2017-2018 (for fiscal year 2018-2019 transfer) for the purposes set forth in Act 14 of 1987.

The amount of the liabilities established to the DDAP were $2,500 and $2,500 for the fiscal years ended June 30, 2018 and June 30, 2017, respectively.

NOTE J – OPERATING TRANSFER FOR LIQUOR CONTROL ENFORCEMENT

The PLCB provides the funding for the Pennsylvania State Police, Bureau of Liquor Control Enforcement, which is responsible for enforcing the laws and regulations governing the trafficking of alcoholic beverages throughout the Commonwealth. The transfers were $30,528 and $28,107 for the fiscal years ended June 30, 2018 and June 30, 2017, respectively.

NOTE K – CONTINGENCIES-LITIGATION

The PLCB is a defendant in various legal proceedings pertaining to matters normally incidental to routine operations. For the fiscal year ended June 30, 2018 the PLCB reported accrued liabilities of $650 with respect to two litigation cases for which the likelihood of an unfavorable outcome is probable and estimable. The probability of an adverse decision and/or damage assessment for all other litigation matters is indeterminate. Based on the current status of these legal proceedings, it is the opinion of the PLCB's management and counsel that they will not have a material effect on the PLCB's financial position. For the fiscal year ended June 30, 2017, there were no accrued liabilities related to litigation.

NOTE L – STATEMENT OF CHANGES IN FIDUCIARY NET POSITION

The Statement of Changes in Fiduciary Net Position illustrates the net asset activities throughout each fiscal year for the Liquor License Fund.

Cash additions include cash received from license application fees as well as cash resulting from the sale of temporary investments. Cash deductions include the purchase of temporary investments as well as cash remitted to the municipalities.

Temporary investments' additions and deductions result from the purchase and sale of securities.

Due to municipalities' additions include monies received from license application fees. Due to municipalities' deductions include payments remitted to municipalities.

NOTE M – SELF-INSURANCE LIABILITIES

The Commonwealth is self-insured for statutory workers' compensation, which includes indemnity and medical payments (employee disability) for its employees injured on the job. The Commonwealth is also self-insured for annuitant medical/hospital claims and for tort liability claims. Major tort risks include automobile, employee and general torts. For property losses, the Commonwealth has a $1 million retention with excess commercial insurance coverage up to $1 billion per occurrence. There was no reduction in commercial insurance coverage during the fiscal year ended June 30, 2018. No settlements exceeded commercial insurance coverage during each of the past three fiscal years. The Commonwealth has established various administrative policies, which are intended to avoid or limit the aforementioned risks.

PLCB participates in each Commonwealth self-insurance program and pays prescribed program amounts or rates throughout its fiscal year. These amounts, reported as current fiscal year expenses, finance a portion of cumulative, estimated self-insurance liabilities incurred, in amounts sufficient to fund ongoing program needs. These amounts do not finance all cumulative, estimated self-insurance liabilities incurred. Therefore, accrued liabilities for employee disability and annuitant medical/hospital claims are established based on reserves computed from the Commonwealth's claim experience; such claims are not discounted and do not include non-incremental claims adjustment expenses.

At June 30, 2018 and June 30, 2017, respectively, the State Stores Fund reported a $55,586 liability ($7,637 as current and $47,949 as non-current) and $48,997 liability ($6,740 as current and $42,257 as non-current) for employee disability claims.

The following summary provides aggregated information for the fiscal years ended June 30, 2018 and June 30, 2017 of the reported self-insurance liabilities to include the incurred claims and payments during the fiscal years then ended:

LIQUOR LICENSE FUND – JUNE 30, 2018 (amounts in thousands)

NOTE M – SELF-INSURANCE LIABILITIES (Continued)

Fiscal Year End	Liability – Beginning Balance	Incurred Claims	Payments	Liability – Ending Balance
June 30, 2018	$48,996	$12,702	$6,112	$55,586
June 30, 2017	$47,059	$7,658	$5,720	$48,997

NOTE N – RESTATEMENT

Effective July 1, 2017, the State Stores Fund implemented the GASB Statement No. 75, "Accounting and Financial reporting for Postemployment Benefits Other Than Pensions". GASB Statement No. 75, replaces GASB Statement No. 45 and establishes accounting and financial reporting standards for OPEB that is provided to employees of state and local governmental employers. This standard establishes standards for recognizing and measuring liabilities, deferred outflows of resources, deferred inflows of resources and expense. The implementation of GASB Statement No. 75 resulted in the reporting of an OPEB liability and deferred outflow of resources, therefore, the State Stores Fund beginning net position has been restated.

Presented below is the change to the State Stores Fund Statement of Net Position as a result of implementing GASB Statement No. 75.

	State Stores Fund
Net Position, as previously reported, at June 30, 2017	$ (352,479)
Apply GASB Statement No. 75	
OPEB Liability	$ (751,633)
Deferred Outflows	$ 26,157
Total Prior Period Adjustment	$ (725,476)
Net Position, as restated, at July 1, 2017	$ (1,077,955)

Fiscal year ended June 30, 2017 amounts are not restated because the GASB Statement No. 75 required actuarial data is not available.

REQUIRED SUPPLEMENTARY INFORMATION

Pension Schedules

Schedule of PLCB's Contributions *(Dollar Amounts in Thousands)*

Last Ten Fiscal Years Ended June 30 (1)

	2018	2017	2016	2015
Contractually required contribution (2)	$ 48,227	$ 40,348	$ 33,752	$ 27,044
Contributions in relation to the contractually required contribution	$ 48,227	$ 40,348	$ 33,752	$ 27,044
Contribution deficiency (excess)	-	-	-	-
PLCB's covered-employee payroll	$171,016	$162,310	$166,701	$162,037
Contributions as a percentage of covered-employee payroll	28.20%	24.86%	20.25%	16.69%

(1) PLCB adopted GASB 68 on a prospective basis for the fiscal year ended June 30, 2015; therefore, only four years are presented in the above schedules. The amounts presented for each fiscal year were determined as of December 31.

(2) The contractually required contribution disclosed above is based on minimum floor rates or suppressed rates resulting from collars that are required based on statutory law. These rates are determined by SERS actuary during the annual funding valuation and include an adjustment to the "preliminary employer contribution rate" calculated before the minimum floor or collars are applied. These "final employer contribution rates" fall within the realm of an appropriate ADC calculation under actuarial standards of practice and temporarily defer a portion of the payments that work towards fully funding the plan.

REQUIRED SUPPLEMENTARY INFORMATION (continued)

Schedule of PLCB's Proportionate Share of the Net Pension Liability *(Dollar Amounts in Thousands)*

Last Ten Fiscal Years Ended June 30 (1)

	2018	2017	2016 (2)	2015
PLCB's proportion of the net pension liability	2.55%	2.48%	2.47%	2.44%
PLCB's proportionate share of the net pension liability	$440,677	$477,444	$ 449,176	$ 362,685
PLCB's covered-employee payroll	$171,016	$162,310	$ 166,701	$ 162,037
PLCB's proportionate share of the net pension liability as a percentage of its covered-employee payroll	257.68%	294.16%	269.45%	223.83%
Plan fiduciary net position as a percentage of the total pension liability	62.97%	57.80%	58.90%	64.80%

(1) PLCB adopted GASB 68 on a prospective basis for the fiscal year ended June 30, 2015; therefore, only four years are presented in the above schedules. The amounts presented for each fiscal year were determined as of December 31.

(2) Every five years, SERS is required to conduct an actuarial experience study to determine whether the assumptions used in its annual actuarial valuations remain accurate based on current and anticipated demographic trends and economic conditions. The 18th Investigation of Actuarial Experience study for the period 2011 – 2015 was released in March 2016 and can be viewed at www.sers.pa.gov. The actuary, under oversight of the SERS Board, reviewed economic assumptions (such as the assumed future investment returns and salary increases) as well as demographic assumptions (such as employee turnover, retirement, disability, and death rates). Some assumption adjustments increased projected cost and some decreased projected cost, but the overall result was an increase to the net pension liability.

REQUIRED SUPPLEMENTARY INFORMATION (continued)

OPEB Schedules

Schedule of PLCB's Contributions *(Dollar Amounts in Thousands)*

Last Ten Fiscal Years Ended June 30 [1]

	2018
Contractually required contribution [2]	$ 29,409
Contributions in relation to the contractually required contribution	$ 26,157
Contribution deficiency (excess)	$ 3,252
PLCB's employee covered payroll	$124,980
Contributions as a percentage of covered-employee payroll	20.93%

[1] PLCB adopted GASB 75 on a prospective basis for the fiscal year ended June 30, 2018; therefore, only one year is presented in the above schedule. The amounts presented were measured as of June 30th of the prior year.

[2] Contribution requirements for the REHP are determined annually by the Commonwealth based on projected cash flow requirements and a projected contribution toward pre-funding future cash outlays.

REQUIRED SUPPLEMENTARY INFORMATION (continued)

OPEB Schedules

Schedule of PLCB's Allocated Share of the Net OPEB Liability *(Dollar Amounts in Thousands)*

Last Ten Fiscal Years Ended June 30 (1)

	2018
PLCB's allocation of the net OPEB liability	3.96%
PLCB's allocated share of the net OPEB liability	$ 793,355
PLCB's employee covered payroll	$ 124,980
PLCB's allocated share of the net OPEB liability as a percentage of its employee covered payroll	634.79%
Plan fiduciary net position as a percentage of the total OPEB liability	1.39%

(1) PLCB adopted GASB 75 on a prospective basis for the fiscal year ended June 30, 2018; therefore, only one year is presented in the above schedule. The amounts presented were measured as of June 30th of the prior year.

Commonwealth of Pennsylvania
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EUGENE A. DePASQUALE
AUDITOR GENERAL

Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance With *Government Auditing Standards*

<u>Independent Auditor's Report</u>

The Honorable Tom Wolf
Governor
Commonwealth of Pennsylvania
Harrisburg, PA 17120

The Honorable Tim Holden
Chairman
Pennsylvania Liquor Control Board
Harrisburg, PA 17124

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the accompanying Statements of Net Position, Statements of Revenues, Expenses and Changes in Net Position, and Statements of Cash Flows for the State Stores Fund, and the Statements of Fiduciary Net Position and Statements of Changes in Fiduciary Net Position for the Liquor License Fund of the Pennsylvania Liquor Control Board (PLCB) as of and for the years ended June 30, 2018 and 2017, and the related notes to the financial statements and have issued our report thereon dated November 28, 2018.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered PLCB's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of PLCB's internal control. Accordingly, we do not express an opinion on the effectiveness of PLCB's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the PLCB's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies, material weakness or significant deficiencies may exist that were not identified. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. We did identify a certain deficiency in internal control, described in the accompanying finding section as Finding No. 1, that we consider to be a significant deficiency.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the PLCB's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards.*

Purpose of This Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of PLCB's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering PLCB's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

November 28, 2018

Eugene A. DePasquale
Auditor General

Finding No. 1– General Computer Controls Need Improvement

Condition: Our review of general computer controls at PLCB for the fiscal year ended June 30, 2018, disclosed the following internal control deficiencies:

1. User account access for six Oracle Point of Service (POS) administrators was not revoked for an unreasonable period after they no longer required this elevated access.

2. User account access for one database administrator was not removed from the Robocom Inventory Management System (RIMS) application database until seven months after he separated employment from PLCB.

Criteria: Management Directive 325.12, *Standards for Internal Control for Commonwealth Agencies*, effective July 1, 2015, adopted the internal control framework outlined in the United States Government Accountability Office (GAO), *Standards for Internal Control in the Federal Government (Green Book)*, published in September 2014.

- Green Book Principle 11 – Design Activities for the Information System, states in part:

    - *11.12 …Management designs control activities over access to protect an entity from inappropriate access and unauthorized use of the system. These control activities support appropriate segregation of duties. By preventing unauthorized use of and changes to the system, data and program integrity are protected from malicious intent (e.g., someone breaking into the technology to commit fraud, vandalism, or terrorism) or error.*
    - *11.14 …Management designs other control activities to promptly update access rights when employees change job functions or leave the entity…*

- Green Book Principle 16 – Perform Monitoring Activities states that *Management should establish and operate monitoring activities to monitor the internal control system and evaluate the results.*

- Green Book Principle 17 – Evaluate and Remediate Deficiencies states that *Management should remediate identified internal control deficiencies on a timely basis.*

Additionally, general control activities over technology are integral to the overall internal control structure of the Commonwealth. A well-designed system of internal controls dictates that IT general controls be established and functioning to ensure that overall PLCB operations are conducted in accordance with management's intent.

Finding No. 1 – General Computer Controls Need Improvement (Continued)

Cause: For the six POS administrators whose privileged access was not removed at the time their job responsibilities changed, the procedures in place to revoke elevated access were not followed appropriately. Additionally, PLCB management did not identify the inappropriate access during their quarterly privileged access reviews because the reviewer (Business Owner) did not have knowledge of the users' current job responsibilities when performing the review.

As for the RIMS separated user whose privileged access was not revoked, PLCB management indicated that the user was initially granted access prior to the implementation of PLCB's in-house access tracking system. Consequently, when the user retired, the tracking system failed to identify the need for access removal. Further, the RIMS application was not subjected to quarterly privileged access review since PLCB management indicated that personnel changes within RIMS are rare.

Effect: Excessive privileged access increases the risk of unauthorized configuration changes, inappropriate transactions, or unapproved alteration of the software. While PLCB management corrected the control weaknesses immediately upon notification by the auditors, failure to downgrade privileged access when users' responsibilities change or revoke access when the users separate employment could result in unauthorized actions in the system. Additionally, computer and other agency operations may not be conducted in accordance with PLCB management's intent.

Recommendation: We recommend that PLCB management:

1. Ensure controls are operating effectively to notify the Security Administrator when users separate employment or when users no longer require privileged access due to changes in job responsibilities.
2. Update the PLCB in-house access tracking system to include all employees with privileged access, including those hired prior to the implementation of the tracking system.
3. Ensure the scope of the quarterly privileged access review includes all critical applications.
4. Ensure that reviewers and approvers performing periodic access reviews confirm users' access is commensurate with their current job responsibilities.

Management Response: The PLCB understands the risk of internal control deficiencies and has added steps to enforce Principal 11 – Design Activities by modifying the privileged account review process.

Finding No. 1 - General Computer Controls Need Improvement (Continued)

Condition:

1. Administrative access to Oracle Point of Service (POS) systems were correctly granted when the individuals in question were assigned to Store Operations. When reassigned to retail store positions the appropriate ITS personnel were unaware of the transfer and the business owner who reviews and approves privileged access to POS wasn't personally familiar with the names presented.

   This has been addressed and corrective action applied; POS business owner will research any unfamiliar name prior to approving continued access during the quarterly review.

2. RIMS local account not removed after personnel retirement.

   This was an oversight due to the very limited number of RIMS users. The risk was low due to RIMS login being restricted to PLCB internal networks and the retired employee no longer had the ability to log into an agency workstation, therefore RIMS could not be reached by this individual.

   RIMS has since been added to the scheduled review, and HR actions will reviewed closely by the Security team for separations and transfers and appropriate actions taken.

Recommendations:

1. In addition to reviewing HR separation and transfer actions, each business owner is required to validate the list of privileged users to the system of their responsibility.
2. All systems requiring administrative access have been added to the quarterly review. Administrators are identified internally from each system and lists of privileged users are presented to the appropriate business owner for review and approval. Changes noted are executed immediately.
3. See #2.
4. Privileged users not known personally by the business owner will be researched and validated, or will be removed immediately.

<u>Auditors' Conclusion</u>: PLCB agrees with the finding. We will review any corrective action in the subsequent audit.

COMMONWEALTH OF PENNSYLVANIA
PENNSYLVANIA LIQUOR CONTROL BOARD
JUNE 30, 2018
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House Liquor Control Committee

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