

May 2021
Report of the Auditor General
to the Nova Scotia
House of Assembly



Nova Scotia Liquor Corporation
– Phase II



Performance Report
Independence • Integrity • Impact

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May 25, 2021

Honourable Kevin Murphy
Speaker
House of Assembly
Province of Nova Scotia

Dear Sir:

I have the honour to submit herewith my Report to the House of Assembly under Section 18(2) of the Auditor General Act, to be laid before the House in accordance with Section 18(4) of the Auditor General Act.

Respectfully,

A handwritten signature in blue ink that reads "Kim Adair-MacPherson".

Kim Adair-MacPherson, FCPA, CA, ICD.D

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Table of Contents

Nova Scotia Liquor Corporation – Phase II	7
Recommendations at a Glance	8
Product Management.....	9
Governance.....	20
Appendix I: Reasonable Assurance Engagement Description and Conclusions	28

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Nova Scotia Liquor Corporation – Phase II

Key Messages

- There are inadequate processes and support for many decisions related to how beverage alcohol products are selected for sale, priced and promoted.
- Physical beverage alcohol inventory is well managed.
- Governance processes are in place and working as intended, with some improvement required.

Why We Did This Audit

- NSLC is significant to the provincial economy.
- In 2019-20, NSLC had \$726.2 million in sales and \$247.3 million in earnings.
- Since 2015, the local alcohol manufacturing industry in the province has grown rapidly, which has a significant impact on NSLC as the main retailer of alcohol in the province.
- We reported Phase I of our audit in June 2020 which identified some areas of concern.

No clear processes or documentation for product management decisions

- Decisions around what alcohol products to sell, the price charged, where to place them in the store and participation in promotional programs are not supported by clear processes
- Improved documentation and retention of support for decision-making required
- Elevated organizational risks due to lack of approvals, review processes, policies, and procedures

Controls over physical inventory operating as intended

- Receipt and distribution of inventory from the warehouse is well managed
- Processes to account for damaged and expired beverage alcohol products are followed

Governance structures and processes in place to provide oversight and accountability

- Board of Directors and its committees generally completed all roles and responsibilities
- Clearer communication of legislated mandate and government priorities sought
- Minor improvements required in some areas, such as board evaluations and review of competencies



Recommendations at a Glance

Recommendation 1.1

The Nova Scotia Liquor Corporation should document policies and procedures for general list and one-time only beverage alcohol product selection, including a document retention policy for information which supports decision making.

Recommendation 1.2

The Nova Scotia Liquor Corporation should develop a management review process to assess if product listing decisions are appropriate and adequately supported.

Recommendation 1.3

The Nova Scotia Liquor Corporation should implement a process to monitor pricing at local manufacturer retail stores.

Recommendation 1.4

The Nova Scotia Liquor Corporation should develop documented policies and procedures for promotional programs, including documentation of the application, decision making, and approval communication process.

Recommendation 1.5

The Nova Scotia Liquor Corporation should review and update the shelf management process, including roles and responsibilities for allocating products to shelves in alignment with NSLC goals, review processes at head office and the retail stores, and documentation and retention requirements.

Recommendation 1.6

The Nova Scotia Liquor Corporation should implement fraud training for all employees.

Recommendation 1.7

The Nova Scotia Liquor Corporation should develop a process to ensure job descriptions are in place for all employees, including the Vice President of Customer Strategy, the Category Director, and the Team Leads.

Recommendation 1.8

The Department of Finance and Treasury Board should develop a process for ensuring government priorities, as they pertain to the NSLC, are clearly documented and effectively communicated to the organization on a regular basis.

Recommendation 1.9

The Board of Directors should ensure that action items are clearly and consistently documented in meeting minutes for the Board and its committees, with updates on their status and final resolution provided at subsequent meetings.

Recommendation 1.10

The Board of Directors should review processes in place to ensure responsibilities that support the effective operation of the board, such as board evaluations, individual member assessments and education sessions, are completed as required.

Recommendation 1.11

The Board of Directors should ensure that its competency matrix is updated in advance of board vacancies, with identified skills gaps communicated to government for consideration during the appointment process.

Nova Scotia Liquor Corporation – Phase II

Product Management

➡ Policies and procedures lacking in many stages of product management

- 1.1 Overall, we found the Nova Scotia Liquor Corporation (NSLC) does not have adequate processes and documentation to ensure important decisions over the procurement and promotion of retail beverage alcohol products are made and supported in a consistent manner.
- 1.2 For an organization of this size, we would expect to see established and well documented policies and procedures in all the key product management business functions at NSLC head office. However, we did not find policies or procedures in the areas of product management that we audited.
- 1.3 The scope of our audit included the selection of beverage alcohol products to sell in stores, as well as pricing, shelf management and promotional program decisions. Generally, we found processes in place lacked clarity; document retention was not a priority; and approval and review processes were almost nonexistent. What the organization expected staff to do in these areas is not clear.
- 1.4 Taken together, the absence of processes and lack of documentation do not inherently mean that decisions made are incorrect. However, unsupported decisions are more likely to arise when there are no documented processes through which they might be questioned or challenged. Clear expectations and documentation requirements supporting these important decisions are essential to ensure the interests of both the organization and staff are protected.
- 1.5 For many suppliers, having products on the shelves of the main retailer of beverage alcohol in the province is significant. Product listing decisions can have a direct impact on sales and overall success. In this competitive space, where there are constraints on how many products can be listed, it is especially prudent to have clearly documented decision-making processes to support that decisions are in line with the NSLC's strategy and goals.

➡ Product selection process and decisions are not adequately documented

- 1.6 There are no documented policies or procedures detailing the beverage alcohol selection process managed by the Customer Strategy group. This includes the listing of new products, the delisting of existing products, and determining where they are sold. Product selection for NSLC's retail stores



is at the core of the corporation's business. Defined processes are needed to support these decisions to ensure they best serve the needs of Nova Scotians, maximize NSLC's sales, and support other strategic goals.

- 1.7 Currently, to arrive at product selection decisions, management stated that staff are continuously reviewing product performance. Category managers indicated they review sales data, identify gaps in the product mix and price points, and consider other criteria including market, customer, and product trends. However, the approach to conduct and document this analysis needs consistency and accountability.
- 1.8 '*General list products*' are carried regularly by the NSLC, while '*one-time only products*' are items brought in for a specified period. The annual beverage alcohol selection process applies to both types of listings. However, one-time only products can also be added and removed outside of the annual process, making the process less transparent than for general listings.
- 1.9 Each year, NSLC publishes an expression of interest for alcohol beverage products, and suppliers and their agents provide a submission which contains the details of the products they wish to list. Submissions are grouped into categories; generally, wines, spirits, beer, and ready-to-drink products.
- 1.10 Staff indicated that they meet with suppliers and agents throughout the product selection process. These meetings may occur before or after listing submissions are due and there is no set timeframe in relation to the process. Management stated that any supplier or registered representative who makes a meeting request prior to the final listing decisions will be granted a meeting with staff. However, neither meeting minutes nor a record of discussion is kept. Record keeping would support consistent consultation with suppliers on product strategies and assist in relationship management and continuity if there are staffing changes. This would also support both fairness and efficiency in the process.
- 1.11 The rationale to add new general list products is often not clearly documented. We reviewed the selection process for 26 sub-category reviews within the wines, spirits, beer, and ready-to-drink categories over a two-year period. Examples of sub-categories include French wine, Canadian whiskey, and single serve beer. Management explained that there are no retention standards for documents associated with product selection. The absence of a filing system was further complicated by staff turnover in recent years and as a result, it took time for us to collect the documents from staff.
- 1.12 We were unable to clearly identify how listing decisions were made in 19 of 26 sub-category reviews. A few wine categories included a product score and tasting results; however, the other categories contained no clear evaluation or rationale to support decisions.



- 1.13 In addition, the rationale to delist existing products is not always documented. Management provided annual review documents including the sales data of current products and other performance information for 23 of 26 sub-category reviews sampled. However, in seven of 26 sub-category reviews we sampled, there was no clear indication how staff reached delisting decisions.
- 1.14 As stated above, decisions made without process or documentation can be open to challenge. The absence of these standard operating procedures also increases the risk that poor decisions can be made, whether due to unsupported partiality, incomplete information, or items falling through the cracks. None of these outcomes is in the best interest of NSLC or its suppliers.

➡ No management approval or other decision review process

- 1.15 After staff finalize their recommendations, new listing and delisting decisions are shared with team members and management through a presentation. Approval from the Vice President of Customer Strategy and the Category Director is required for all changes to the general list. We were told that the presentation, or a meeting with management, constitutes approval. However, this approval process is not formalized, and is usually not documented. Of the 26 sub-category reviews we tested, there were only four instances of documented approval for sub-category listing changes as presented.
- 1.16 After the presentation, staff create a final listing document to detail all changes to the general list. This document is shared with other operational divisions within the NSLC, including marketing and supply chain. However, we found once again that there is no document retention requirement and the information available varied by category. Moreover, in only one of the 26 sub-category reviews did the final listing document match the recommendation presented to management.
- 1.17 Management explained that in some instances, a listing decision may be changed after the presentation of recommendations. For example, products may have been planned as a one-time only offering and later switched to the general listing (and vice versa), or a supplier may request to make a product change.
- 1.18 In our review, we found at least 58 products in the final listing documents which had not been presented in the recommendations to management. There is no documented explanation for these changes.
- 1.19 Overall, we could not determine the accuracy of the documentation provided throughout the 26 sub-category reviews as there was no employee sign-off or date stamping. Without strong document management controls, management cannot ensure that documents are available to review decision making or determine if there were unauthorized changes by staff.



- 1.20 There is no other process in place to review category manager decisions, including no internal audit involvement. Given the lack of documentation in the current processes, implementing any type of meaningful review process beyond a discussion with the decision maker would be a significant challenge.



One-time only products added throughout the year with no clear approvals

- 1.21 As noted above, one-time only products can be added and removed outside of the annual product selection process. Staff indicated that these situations are handled on a case-by-case basis. As with the expression of interest process, there are no formally documented policies or procedures detailing the selection of one-time only products.
- 1.22 We reviewed a sample of one-time only products for a specified period with staff. We found approvals from other teams within the NSLC, such as pricing and supply chain, clearly documented; however, no approvals or rationale were documented from the Category Management Team for the actual decision to add a product.
- 1.23 In some cases, it was clear that the product was listed as part of a specific program such as a Christmas feature. However, in other cases it was unclear why a product was added as there is no required documentation to list the product.
- 1.24 The absence of controls creates an environment for decision making which does not support the goals of the organization and increases the risk of fraud. While we saw no evidence of fraud or employee wrongdoing, the conditions exist which could allow this to occur. Without proper management oversight, there is a risk that poor decisions in the product selection process may not be identified.

Recommendation 1.1

The Nova Scotia Liquor Corporation should document policies and procedures for general list and one-time only beverage alcohol product selection, including a document retention policy for information which supports decision making.

Nova Scotia Liquor Corporation response: The NSLC agrees with this recommendation. The NSLC will document selection criteria, processes, and decisions with rationale. The NSLC will also define a consistent approval process with appropriate oversight and standardize the retention of documents in a central hub with proper date coding. This will be supported by supplier communication that clearly outlines the decision rationale. Timelines: Document the process with selection criteria – July 2021. Document retention process implemented – March 2022.



Recommendation 1.2

The Nova Scotia Liquor Corporation should develop a management review process to assess if product listing decisions are appropriate and adequately supported.

Nova Scotia Liquor Corporation response: The NSLC agrees with this recommendation. The NSLC will develop a review process that tracks, date codes and stores all product listing changes in a central hub. Timeline: March 2022.

➤ Pricing process is not documented

- 1.25 There are no policies or procedures for the pricing review process. An external review of the pricing process was conducted in May 2018, and several of the recommendations for improved controls have since been implemented. Management stated that based on these changes, policies and procedures are now being developed.
- 1.26 Each product category has its own defined and mandatory price band. These price bands are to be reviewed during the semi-annual pricing changes. However, although we saw price band changes within the period of the audit, no documentation was available to support why the bands changed.
- 1.27 We sampled 50 products and found that they were all within the appropriate price band, greater than the social reference price, and approved by the pricing coordinator.

What is a social reference price?

A minimum price according to product category and size, intended to minimize social harm associated with overconsumption.

- 1.28 Although no significant issues were identified, NSLC should document the policies and procedures related to pricing, and ensure the process includes documenting rationale for price band changes.

➤ Pricing at local manufacturer stores not monitored

- 1.29 Local manufacturer retail stores are not supposed to sell product for less than the listed price at NSLC, or below the social reference price if the products are not sold by NSLC. NSLC's Manufacturer's Policy requires that a price list be submitted to the pricing coordinator annually. This process is not happening; no price lists are received by NSLC, and no follow-up is done to obtain the lists or verify appropriate pricing at these local retail outlets.



- 1.30 With the number of local manufacturer retail stores continuing to grow in the province, oversight of this requirement should be established.

Recommendation 1.3

The Nova Scotia Liquor Corporation should implement a process to monitor pricing at local manufacturer retail stores.

Nova Scotia Liquor Corporation response: The NSLC agrees with this recommendation. The NSLC will be expanding the mandate of the retail audit function to include local producers. As part of the audit program selling prices will be reviewed. Timeline: December 2021.



Promotional programs do not have a clear decision-making process

- 1.31 Promotional programs are another area in which we found little to no support for decision making beyond a final list of approved and rejected applications. The Promotions Team administers the program by receiving the applications and providing the approval or rejection decisions to applicants. However, the Category Management Team is mainly responsible for the decision-making process for promoted products.
- 1.32 NSLC publishes an annual promotion guide which it provides to all suppliers. The promotions guide details the promotions that will run for the year and provides guidance on pricing and the application process.
- 1.33 We selected five promotional programs for a more detailed examination. NSLC provided listings of approved and rejected applications for each program and period selected. These listings provide no information on how decisions were made, so we were unable to complete any further work on whether the decisions made were appropriate and in the best interest of the Corporation.
- 1.34 For approved promotions, we found that the vendor was charged the appropriate amount, except for one program which offered discounts for local manufacturers. We found that the discount process is not documented or formally communicated to suppliers. Despite that, we did find the approach was applied consistently for all local applicants sampled. However, this should be clearly communicated to all local manufacturers.

Recommendation 1.4

The Nova Scotia Liquor Corporation should develop documented policies and procedures for promotional programs, including documentation of the application, decision making, and approval communication process.

Nova Scotia Liquor Corporation response: The NSLC agrees with this recommendation. The NSLC will leverage technology to communicate and archive vendor application status as well as formally document promotion consideration criteria and application results. Timeline: July 2021.

➡ Weaknesses identified in shelf management process

- 1.35 There is no approval process or review of shelf plans by anyone at NSLC, including management or the internal audit group. Shelf management is done centrally at NSLC's head office, and individual shelf plans for all 108 stores across the province are the responsibility of one person. Each store receives updated shelf plans nine times per year, corresponding to NSLC's nine promotional periods.

What is a shelf plan?

A shelf plan is a diagram which indicates the placement and number of facings of retail products on shelves, generally intended to maximize sales. Facings refer to the number of bottles of the same product visible to the consumer from the front when shopping (for example, there are three facings of the wine bottle with orange label featured below).



- 1.36 Shelf placement can influence product sales, which may affect the achievement of NSLC's goals, and suppliers' performance, which may impact their future listings. Therefore, it is important that processes align with NSLC's strategies and that processes are followed.
- 1.37 There is a shelf management process manual which has not been updated since 1999. The manual documents how products are assigned a location and are given a number of facings on the shelf. It also includes directions on how the store should implement the plan. Since the manual's creation over 20 years ago, there have been many changes to the process and it no longer accurately reflects the processes in place.
- 1.38 Each product position is to be reviewed at least once a year to move products with poor sales and allow the opportunity for other suppliers to improve

their shelf position. The shelf management specialist stated that facings are determined based on sales over the past 12 months.

- 1.39 The data used to make these decisions is reviewed at a point in time in a live system, and not documented. The process is not adequately documented to allow a second person to confirm the process was completed accurately. It should require, at a minimum, date and time stamping to support the verification and accountability of the decision-making process.

 Store implementation of shelf plans is not verified for accuracy

- 1.40 When a store implements a shelf plan, the action is indicated in the shelf management system by the store manager. We visited six stores to verify if a pre-selected sample of shelf plans were implemented accurately and found many differences in the execution.
- 1.41 In every store we visited, we found several areas where the products and number of facings did not match the shelf plans. In most instances, the number of facings was one or two more or less than it was supposed to be, or products were displayed in the wrong location.
- 1.42 As noted above, the store manager must indicate in the system that the plan has been implemented. However, whether this information is reviewed at head office is not documented, and the completion notification is deleted from the system when a new shelf plan is added.
- 1.43 The shelf management process manual also refers to management overview by the internal audit group as part of their process. However, internal audit management confirmed that this process was discontinued several years ago.
- 1.44 Ensuring the process to create shelf plans is completed as expected and aligns with NSLC's goals is only effective if the plans are implemented at the store level.

Recommendation 1.5

The Nova Scotia Liquor Corporation should review and update the shelf management process, including roles and responsibilities for allocating products to shelves in alignment with NSLC goals, review processes at head office and the retail stores, and documentation and retention requirements.

Nova Scotia Liquor Corporation response: The NSLC agrees with this recommendation and will review, update, and document shelf management principles, responsibilities, and processes to reflect the current dynamic of the business. As well, formal approval processes for planogram concepts will be established and documented.



In addition, the NSLC will establish a document retention process for this area and implement a shelf management review process at retail stores performed by regional directors and through internal audit. Timelines: Shelf management process document – July 2021. Document retention and review process – August 2021.

➡ Weaknesses in fraud training and conflict of interest disclosure

- 1.45 There is no mandatory fraud training in place for employees. We did note that the NSLC conducted a fraud risk assessment in July 2017 and subsequently implemented a fraud policy in October 2017. For the year ending in March 2020, the NSLC posted sales of \$726 million and strong fraud prevention practices should be in place to safeguard provincial revenues and assets.
- 1.46 The NSLC does have both a Code of Business Conduct and a Conflict of Interest Policy to provide guidance to all employees regarding personal and business relationships, employment, and accepting gifts. The policy dictates that no employee may accept a gift or benefit that could reasonably be perceived to have influenced the individual in the performance of their duties.
- 1.47 To ensure employees understand and are aware of their responsibilities under the Code of Conduct and Conflict of Interest, employees are required to complete training in the NSLC learning system every two years. We sampled ten employees and found that all ten had completed their initial training; however, two employees did not meet the two-year training recertification requirement. Management indicated that the issue has been corrected and employees and supervisors will now receive a notification to update their training on a regular basis.
- 1.48 Although there is a Conflict of Interest form in place which provides clear direction to employees on how to disclose a conflict of interest when one arises, the process relies on the employee to actively self-disclose. NSLC does not proactively require periodic confirmation that no conflicts exist.
- 1.49 While a conflict of interest does not necessarily indicate wrongful conduct, when disclosed, controls can be put in place to ensure there is no impact on the product selection process.
- 1.50 We sampled ten employees who are involved in the category management process and enquired if they had Conflict of Interest forms on file. None of the ten had a disclosed conflict of interest. Therefore, there were no samples that required verification that appropriate measures were put in place to address a conflict. NSLC should evaluate whether the current approach to disclosure is appropriate for all positions, or if annual representations should be implemented in some cases.



- 1.51 With the lack of clear processes, documentation and approvals in the product selection process, strong fraud and conflict of interest measures are important due to the greater opportunity to make unsupported decisions.

Recommendation 1.6

The Nova Scotia Liquor Corporation should implement fraud training for all employees.

Nova Scotia Liquor Corporation response: The NSLC agrees with this recommendation and has already developed a fraud training program for all employees, which employees will be required to take every 2 years. This will be monitored for compliance by managers. Timeline: Implemented as of April 2021.



Roles and responsibilities supporting product selection are not defined

- 1.52 We reviewed the NSLC organization chart and found there are no formal job descriptions for several employees who hold management level positions in the Customer Strategy division, including the Vice President of Customer Strategy, the Category Director, and the Team Leads. Employees in these positions are responsible to implement, oversee, and approve the product selection process. Job descriptions are in place for category managers, who are responsible for managing product categories and their performance, including the product listing decisions discussed above.
- 1.53 Job descriptions define the roles and responsibilities for each employee, including the deliverables and how each role aligns with organizational goals and objectives. Without job descriptions, it is challenging for management and the Board of Directors to ensure that employees are fulfilling deliverables or can be held accountable for their decisions and oversight duties. For example, the lack of a clear approval or review process over product listings could potentially be a result of the lack of clearly defined roles and responsibilities at the management levels.

Recommendation 1.7

The Nova Scotia Liquor Corporation should develop a process to ensure job descriptions are in place for all employees, including the Vice President of Customer Strategy, the Category Director, and the Team Leads.

Nova Scotia Liquor Corporation response: The NSLC agrees with this recommendation and will have job descriptions formalized for the roles of VP of Insights and Customer Engagement, Category Director and Category management roles (Sr. Category Manager, Category Manager & Associate Category Manager).

As well, the NSLC is in the process of reviewing and refreshing the formalization of the job description process for all levels of leadership, and staff. Timelines: Job



descriptions for specified positions – May 2021. Job description process formalized – March 2022.



Established physical inventory management controls are working

- 1.54 Generally, when NSLC places an order from a vendor, the beverage alcohol products are delivered directly to the distribution centre in Halifax. NSLC has both manual and electronic controls in place to ensure that orders arriving from vendors contain all items listed on the purchase order. Controls include verification by multiple staff with clearly defined roles, and processes to address any issues identified in receiving.
- 1.55 We tested a sample of 30 receiving packages and found no significant issues with the execution of the receiving process at the distribution centre.
- 1.56 When an order is placed from the retail store level, the inventory is prepared at the distribution centre and delivered to the store. Orders are sealed once they are loaded on the truck, and the seal is broken by staff receiving the order at the store.
- 1.57 Periodic order reviews are scheduled by head office and completed at the retail store. To complete an order review, staff must count every item received and complete a template report on the results. Any deviations from expectation are then investigated with the distribution centre.
- 1.58 We tested a sample of 30 order reviews and found that the counts were completed, including all required reporting, and follow-up and adjustments to inventory were completed when required.
- 1.59 Another key part of inventory management is properly accounting for product which is broken, expired or otherwise unavailable to sell. NSLC has documented procedures in place for how to address these issues when they arise, including a breakage log template.
- 1.60 The breakage log must be signed by two staff members and include one of several codes to identify what happened to the product. These logs must be retained at the store, and the internal audit group includes breakage audits as part of their annual audit plan.
- 1.61 One hundred and five breakage logs were selected for inspection across 20 NSLC retail stores, and we found the process was followed, with a few minor issues identified.
- 1.62 As opposed to the processes for selection, promotions and shelf management, the inventory management processes in the distribution centre and retail stores were very well documented and organized with compliance processes in place which are assessed regularly.



Governance

➔ Improved communication of government priorities and objectives in relation to the NSLC needed

1.63 The NSLC does not receive an annual mandate letter or other formal communication of government's current priorities as they relate to the NSLC. The overall mandate is communicated by government through the Liquor Control Act and the Cannabis Control Act and is in some areas conflicting if there is not additional direction to the Board of Directors on government's expectations and prioritization. The objectives of the NSLC as defined in the Acts include the:

- promotion of social objectives regarding responsible drinking and consumption of cannabis;
- promotion of industrial or economic objectives regarding the beverage alcohol industry in the province;
- attainment of suitable financial revenues to government;
- attainment of acceptable levels of customer service; and,
- controlling and carrying out the purchase, possession, distribution, and sale of cannabis.

1.64 The Minister of Finance and Treasury Board is responsible for overseeing the administration of the NSLC. The Acts outline the types of decisions that are subject to approval by government. For example, which municipalities may sell liquor and where agency stores may operate by permit.

1.65 The Board of Directors communicates recommendations for changes to legislation through the Chair of the Board, who meets quarterly with the CEO and Minister. Additionally, opportunities arise for discussion with the Deputy Minister, who is a non-voting board member and attends all meetings.

1.66 In the context of public policy considerations, government can also exercise its authority over additional decisions beyond those outlined in the Acts. For example, the decision to expand the reduced markup offered to local craft brewers producing less than 15 thousand hectolitres to all local producers regardless of size to a capped amount was a decision of government communicated by the Deputy Minister in a board meeting. There was no specific consultation process with the Board of Directors or NSLC's management and no written directive or outline. The board approved this policy at their February 12, 2020 meeting.

1.67 Through interviews with members of the board and senior management, the relationship with the Department of Finance was rated positively. However,



it was noted that consideration should be made for the Minister to attend a board meeting once a year and develop a mandate letter to outline government objectives and priorities. Similar concerns were also raised as part of the 2018 board evaluation discussed later in the report.

- 1.68 Effective communication by government is important to ensure decisions made at the NSLC are in alignment with government objectives and priorities. For decisions not specifically subject to approval by Government, increased consultation and communication with the board and senior management could reduce the need for government involvement.

Recommendation 1.8

The Department of Finance and Treasury Board should develop a process for ensuring government priorities, as they pertain to the NSLC, are clearly documented and effectively communicated to the organization on a regular basis.

Department of Finance and Treasury Board Response: The department is pleased that the NSLC board and management view the relationship with Finance and Treasury Board as positive and will continue to maintain and strengthen the relationship. The Shareholder already provides direction to the NSLC through the development process of its five-year strategic plan and annual business plans. For both plans, there is already a regular process whereby the Minister and Deputy Minister provide mandate feedback and direction on the draft plans, prior to these plans being approved by the Board of Directors. After approval of the annual business plan, there may be in-year issues that require direction by the Shareholder and these are communicated by the Minister directly or through the Deputy Minister to the Chair and/or Board of Directors. As required, the department will document when the Shareholder direction is provided.

➡ Board of Directors appropriately completed their governance responsibilities

- 1.69 Overall, the Board of Directors and its committees held meetings on a regular basis from 2017 to 2019, discussed matters relevant to their terms of reference, and conducted their roles and responsibilities in a timely manner.
- 1.70 The Board of Directors consists of nine voting directors and two non-voting directors. Non-voting directors are the President and CEO of the NSLC and the Deputy Minister of Finance. The board has the following committees:
- Audit and Risk
 - Corporate Social Responsibility
 - Governance and Human Resources



Source: mynslc.com, December 2020

1.71 The roles and responsibilities of the Board of Directors have been documented through legislation, the Board Governance Charter, Committee Charters and annually approved workplans. Through interviews with members of the board, we found that members understood their roles and responsibilities, described the board as effective, and felt they could challenge or debate other directors and management during meetings.



Resolution of board and committee action items not documented

1.72 Action items were not consistently documented and followed up on at the board or committee level. For example, at the committee level, the Governance and Human Resources and the Corporate Social Responsibility meeting minutes each contain sections which list items requiring further action to be taken. Only the Corporate Social Responsibility Committee included follow-up status updates at subsequent meetings to confirm that action items were acted on and resolved.

1.73 The Audit and Risk Committee and the Board of Directors did not include an action item section in their meeting minutes and therefore, action items were not always clearly identifiable. Additionally, subsequent minutes did not contain status updates of items or their final resolution. Resolution of action items is done informally through discussions at agenda planning meetings held between the Chair of the Board or Chair of the Committee, the Corporate Secretary, and a member of the Executive Team.

1.74 Action items should be documented consistently in meeting minutes so the board and its committees are clear when further actions are required and who is responsible. Updates to the board or committee, along with documentation of their resolution, strengthens accountability and ensures items are resolved appropriately to the satisfaction of board and committee members.

Recommendation 1.9

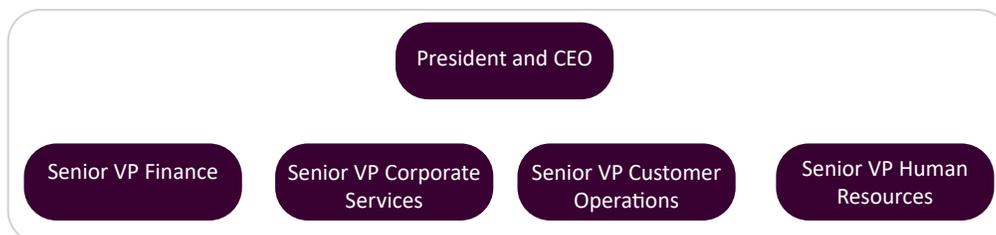
The Board of Directors should ensure that action items are clearly and consistently documented in meeting minutes for the Board and its committees, with updates on their status and final resolution provided at subsequent meetings.



Nova Scotia Liquor Corporation response: The NSLC agrees with this recommendation. The NSLC has created a follow up action document to track all actions items coming out of committee and board meetings. Timeline: Implemented as of February 2021.

➔ Executive Team completed its accountabilities to the Board of Directors and Department of Finance

- 1.75 For 2017 to 2019, the Executive Team fulfilled its accountabilities in a timely manner to the Board of Directors and the Department of Finance and Treasury Board.
- 1.76 The Executive Team has five members with the President and Chief Executive Officer and four Senior Vice Presidents. While some individuals are relatively new to their positions, all current members of the executive are experienced and understand their roles and responsibilities. The Senior Vice President Human Resources was in the process of being filled at the time we completed our audit work.



Source: *mynslc.com*, December 2020

➔ Members of the Executive Team do not have job descriptions

- 1.77 Job descriptions do not exist for four of the five members of the Executive Team. While a job description exists for the CEO that aligns with the mandate, mission, and vision of the NSLC, it has not been updated since 2016. It was not updated in 2019 when a new CEO was hired. NSLC should ensure current job descriptions are in place for all employees, as previously recommended in this report.
- 1.78 Through a review of two executive management committees, it was noted that roles and responsibilities of the committees were documented through terms of reference. These committees were held accountable through the recording of meeting minutes and discussed matters relevant to their terms of reference. However, standing agenda items were not always covered, and meetings were not consistently held at the frequency defined. One of these committees has since been dissolved. For the committee that is still in place, it is important that the terms of reference are reviewed regularly so that they reflect current practices to ensure responsibilities are executed appropriately and outcomes achieved.



Frequency of board evaluations not in accordance with policy

- 1.79 The Board of Directors does not conduct annual evaluations of its overall performance. During 2017 to 2019, an evaluation was only conducted for 2018.
- 1.80 The Charter of the Governance and Human Resources Committee assigns responsibility for developing an annual process for the board's evaluation of its own performance. The process to be followed for the annual evaluation is not formally documented. A clearly defined process would help ensure the evaluation is completed consistently at required intervals.
- 1.81 The evaluation conducted in 2018 was administered by a third-party research company. The evaluation included an assessment of the board itself, its committees, and individual members. Results were compiled in a summary report and discussed at the Governance and Human Resources Committee and at the board level. Planned actions for improvement were identified, including two future education sessions. However, neither education session was held. It is important that planned actions in response to the results of evaluations be taken to ensure continuous improvement of the board and its committees.

Individual board member development plans are not documented

- 1.82 The board does not document individual board member development plans. The Charter for the Governance and Human Resource Committee indicates the committee is responsible for compiling board member development plans annually. They are completed verbally between the Chair of the Committee and each individual member. Since they are not documented, we were unable to confirm whether these occurred. It is important that development plans are documented to identify any areas for improvement and to hold each board member accountable for personal development.

Orientation process is in place however, further education sessions not occurring as expected

- 1.83 The board has a documented orientation process that is reviewed annually by the Governance and Human Resource Committee. Through interviews, board members confirmed that they received orientation in a timely manner following their appointment to the board.
- 1.84 Following appointment, limited education sessions were held at the overall board level for all members. Annual workplans for the board contained an education session placeholder for most meetings with details to be determined. However, only one session was held each year.



- 1.85 During 2017 to 2019, the Board of Directors was very busy overseeing the introduction of cannabis at NSLC stores, as well as the recruitment and hiring of a new CEO. However, in the future they should consider opportunities for education sessions, which will keep members up to date on governance best practices and other topics relevant to the organization. During interviews with board members, suggestions for ongoing training included: sessions on local industry, cybersecurity, and governance.

Recommendation 1.10

The Board of Directors should review processes in place to ensure responsibilities that support the effective operation of the board, such as board evaluations, individual member assessments and education sessions, are completed as required.

Nova Scotia Liquor Corporation response: The NSLC agrees with this recommendation. The NSLC's board evaluation process, which includes individual member assessments, has been added to the Governance and Human Resources (GHR) workplan and will be performed on an annual basis. This year's board evaluation was launched in February 2021. The individual member assessments will be documented by Board Chair and GHR Chair and the evaluation results will be discussed in June 2021 at committee and board meetings. The board education planning process will take place on an annual basis. The board education sessions are planned out for fiscal year 2022. Timeline: June 2021.



Documented CEO evaluation process is in place

- 1.86 The annual goal setting and CEO evaluation process was documented and approved by the Board of Directors in February 2018. The Chair of the Board and the Chair of the Governance and Human Resource Committee are jointly responsible for executing this process.
- 1.87 While the process was not formalized until 2018, an evaluation was conducted for the 2017-18 fiscal year. Deficiencies identified in this evaluation cycle included: performance objectives not being documented at the beginning of the year, and lack of documentation or retention of feedback solicited from board members and industry on the CEO's performance. An evaluation was not conducted in 2018-19 due to the departure of the previous CEO.
- 1.88 The 2019-20 evaluation was completed in accordance with the established process, with minor deviation due to the transition to a new CEO who was appointed in May 2019. Goals of the outgoing CEO were carried forward for use in the 2019-20 evaluation cycle, which were based on priorities identified in the annual business and strategic plans. We encourage the Board of Directors to ensure that future evaluations continue to be conducted in accordance with the established process and are documented.



Appointments and re-appointments to the Board of Directors were appropriate

- 1.89 Governor in Council is responsible for approving appointments to the board based on established selection criteria. All members have experience in at least one of the required selection criteria areas:



- 1.90 In total, four new appointments to the board occurred between 2017–2019. The appointments were generally completed on a timely basis, taking on average 57 days to fill a vacancy. Operational vacancies do not exist as members of the board remain in office beyond the expiry of their term until they are re-appointed or replaced as required by Section 7(7) of the Liquor Control Act.
- 1.91 Between 2017 and 2019, the terms of four members expired and resulted in re-appointment. Confirmation of re-appointments took longer than new appointments, ranging from 95 to 337 days to confirm. The rationale for these delays included: impacts due to a Ministerial transition, an election call in 2017, and cancellations of the HR Committee due to the COVID-19 Public State of Emergency. Like new appointments, there was no operational vacancy as each member whose term had expired remained in office until their re-appointment was confirmed.

Board competency matrix has not been updated since 2017

- 1.92 The Charter for the Governance and Human Resources Committee includes an annual assessment of board member skills and experience. In Fall 2017, a Director Competency Matrix was prepared. However, it has not been updated since then and does not reflect the current membership of the board.
- 1.93 Through interviews with board members and senior management, concerns were raised regarding succession planning of board members as terms expire. Specifically, gaps in IT and legal expertise were identified. Additionally, the Audit and Risk Committee Charter requires that at least one of its members shall be an audit committee expert and meet defined criteria. Presently, this requirement is satisfied through only one member; however, their term expires in 2021. The remaining members of the committee would not satisfy this requirement and therefore, it is imperative that consideration be given to the audit committee expert criteria when the new appointment is made.



- 1.94 The competency matrix is a good tool to assess and communicate the skill set composition of the board to government. It also identifies gaps and weaknesses, which can be filled through new appointees. The matrix should be updated more frequently so that it is up to date and reflects the current composition of the board when vacancies arise.

Recommendation 1.11

The Board of Directors should ensure that its competency matrix is updated in advance of board vacancies, with identified skills gaps communicated to government for consideration during the appointment process.

Nova Scotia Liquor Corporation response: The NSLC agrees with the recommendation. The Governance and Human Resources (GHR) committee added the review of the competency matrix to the workplan. This review will be performed on an annual basis. Upon this year's review, GHR has identified a need to amend the matrix. This item will be discussed and approved at the June 2021 GHR meeting. Once the change is approved, board members will be asked to fill out the matrix and the results will be discussed at the August GHR meeting and shared with Shareholder subsequently. Timeline: August 2021.

- 1.95 While our overall conclusions on governance were mainly positive, we did identify significant issues with product management in this report. We did not identify anything in our work to indicate that the Board of Directors was aware of these process weaknesses and related risks and failed to act. It will now be important that the Board of Directors is committed, through the governance structures outlined above, to the oversight of management's response to the recommendations in this report.



Reasonable Assurance Engagement Description and Conclusions

In May 2021, we completed an independent assurance report on product management, including selection and promotion, and governance practices at the Nova Scotia Liquor Corporation. The purpose of this performance audit was to determine whether the Nova Scotia Liquor Corporation has strategic and effective processes to support the distribution and sale of beverage alcohol in Nova Scotia.

This chapter is the second of a two-phase audit at the Nova Scotia Liquor Corporation. The first phase was reported in June 2020.

It is our role to independently express a conclusion about whether product management, including selection and promotion, and governance practices comply in all significant respects with the applicable criteria. Management and the Board of Directors at the Nova Scotia Liquor Corporation have acknowledged their responsibility for product management, including selection and promotion, and governance practices.

This audit was performed to a reasonable level of assurance in accordance with the Canadian Standard on Assurance Engagements (CSAE) 3001—Direct Engagements set out by the Chartered Professional Accountants of Canada; and sections 18 and 21 of the Auditor General Act.

We apply the Canadian Standard on Quality Control 1 and, accordingly, maintain a comprehensive system of quality control, including documented policies and procedures regarding compliance with ethical requirements, professional standards and applicable legal and regulatory requirements.

In conducting the audit work, we have complied with the independence and other ethical requirements of the Code of Professional Conduct of Chartered Professional Accountants of Nova Scotia as well as those outlined in Nova Scotia’s Code of Conduct for public servants. The objectives and criteria used in the audit are below:

Objectives:

To determine if the Nova Scotia Liquor Corporation procures and promotes retail beverage alcohol products to meet the demands of Nova Scotians, in a fair and consistent manner.

To determine if the Nova Scotia Liquor Corporation is appropriately managing retail beverage alcohol inventory.

Criteria:

1. The Nova Scotia Liquor Corporation should follow a defined a process for determining product mix and allocation that aligns with the goals and objectives of the organization.
2. The Nova Scotia Liquor Corporation should follow a defined procurement process for beverage alcohol.
3. The Nova Scotia Liquor Corporation should follow a defined process for establishing and reviewing product pricing.
4. The Nova Scotia Liquor Corporation should follow a defined process for the selection of product promotions.
5. The Nova Scotia Liquor Corporation should follow a defined process for the ordering, storage, distribution and tracking of retail beverage alcohol inventory.

**Objectives:**

To determine whether governance structures and processes are in place and working to provide oversight and accountability in support of the achievement of the Nova Scotia Liquor Corporation's mandate.

Criteria:

1. The mandate of the Nova Scotia Liquor Corporation should be clearly defined and communicated by Government.
2. Roles, responsibilities and accountabilities of the Board of Directors and its Committees, the CEO and senior management should be clearly defined, and consistent with achieving the mandate.
3. The Board of Directors and its Committees, the CEO and senior management should complete required actions to fulfil their established roles, responsibilities and accountabilities.

Generally accepted criteria consistent with the objectives of the audit did not exist. Audit criteria were developed specifically for this engagement. Criteria were accepted as appropriate by senior management at the Nova Scotia Liquor Corporation.

Our audit approach consisted of interviews with management, staff and the Board of Directors of the Nova Scotia Liquor Corporation; reviewing policy; examining processes for product management and a detailed file review. We examined relevant processes, reports, meeting minutes and other supporting documentation. Our audit period covered April 1, 2017 – December 31, 2019. We examined documentation outside of that period as necessary.

We obtained sufficient and appropriate audit evidence on which to base our conclusions on May 3rd, 2021, in Halifax, Nova Scotia.

Based on the reasonable assurance procedures performed and evidence obtained we have formed the following conclusions:

- NSLC does not have clear policies and procedures for the procurement and promotion of retail beverage alcohol and does not have sufficient documentation to support fair and consistent decision-making in most instances.
- NSLC is managing their physical beverage alcohol inventory well through the implementation of controls and monitoring processes, which are operating effectively.
- NSLC has governance structures and processes in place to provide oversight and accountability in support of the achievement of the NSLC's mandate which are generally working as intended. However, some improvements were identified.

• • • **Office of the Auditor General** • • •

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