

**MEMORANDUM**

June 10, 2015

**TO:** Ad Hoc Committee on Liquor Control

**FROM:** Craig Howard, Senior Legislative Analyst, OLO  
Leslie Rubin, Senior Legislative Analyst, OLO

**SUBJECT:** Follow-up – OLO Report 2015-6: Review of Alcohol Control in Montgomery County

On June 12, the Ad Hoc Committee on Liquor Control will discuss OLO's memorandum that begins on the next page, *Follow-up to Report 2015-6: Further Analysis of Option 4 – Private Wholesale Distribution of Special Order Beer and Wine*.

OLO Report 2015-6 provided the Council with a continuum of five options for changes to the County's alcohol control structure. The Committee requested that OLO provide additional information on Option 4 at its May 8 worksession.

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Office of Legislative Oversight

SUBJECT: Follow-up to OLO Report 2015-6: Further Analysis of Option 4 – Private Wholesale Distribution of Special Order Beer and Wine

OLO Report 2015-6, *Review of Alcohol Control in Montgomery County*, provided the Council's Ad Hoc Committee on Liquor Control with a continuum of five options for changes to the County's alcohol control structure. At its May 8 worksession, the Committee requested that OLO provide additional information on "Option 4" – allowing private wholesale distribution of special order beer and wine while maintaining County control of the wholesale for stock beer and wine products and the wholesale and retail for all liquor products.

Specifically, the Committee requested an analysis of potential implementation methods and issues if the Council were to endorse this structural change. This memorandum uses information originally published as part of OLO Report 2015-6 as well as additional or updated information provided by the Department of Liquor Control (DLC) or other stakeholders since the report's release. It is organized as follows:

- **Section A** defines special order and stock items within DLC's system, and provides the most recent inventory, sales, and cost/pricing data for special order products;
- **Section B** summarizes the problems and issues identified by licensees related to DLC's current operations and structure for special order products and summarizes feedback from licensees and Maryland wholesalers/distributors related to Option 4;
- **Section C** analyzes two different implementation methods – completely deregulating the special order market ("Open Distribution" method) or allowing private wholesale delivery of special orders ("Drop Ship" method);
- **Section D** analyzes alternatives to replace DLC revenue that may be lost if private wholesalers were able to distribute special order products.

## A. DLC Special Order Products – Definition and Data

All DLC beer, wine, and liquor inventory items are categorized as stock or special order. Stock items “are carried at all times and ordered by DLC on a recurring basis to ensure an appropriate volume is available on hand to fulfill projected retail demand.”<sup>1</sup> Stock products are DLC’s most commonly-purchased items and typically are available in DLC’s warehouse for delivery on a licensee’s next scheduled delivery day. Special order items are not regularly carried as inventory in DLC’s warehouse, but instead are purchased by DLC in response to a specific order from a licensee (or a customer at a DLC retail store). Some stock and special order products, however, are only offered seasonally or in limited quantities by the manufacturer.

DLC has a Product Selection Committee that meets once a month to determine whether products should be carried as stock or special order. The Committee consists of the Chief of Administration, Chief of Operations, one representative from retail store operations, and two representative from the purchasing section. The Committee can decide to make a special order item a stock item, and can also return a product to special order status if it is not selling fast enough as a stock item.

**Number of Special Order and Stock Products.** As of March 3, 2015, DLC’s product list includes 27,491 different beer and wine items available for purchase, with 23,709 (86%) categorized as special order (and potentially impacted by Option 4). As shown in Table 1, around 90% of wine products, 65% of beer products sold in cases (i.e., bottles and cans), and 73% of beer kegs are listed as special order.

**Table 1. Stock and Special Order Beer and Wine Products Listed for Sale by DLC**

Product Type	Total Products	Stock	Special Order
Wine	22,481	2,165 (10%)	20,316 (90%)
Beer – Cases	3,398	1,181 (35%)	2,217 (65%)
Beer – Kegs	1,612	436 (27%)	1,176 (73%)
<b>Total</b>	<b>27,491</b>	<b>3,782 (14%)</b>	<b>23,709 (86%)</b>

Source: DLC

**Special Order Wholesale Sales, Markups, and Profit.** In FY14, special order wine, beer, and liquor products accounted for \$28.2 million (21%) of DLC’s total wholesale sales revenue and 308,327 (7%) of the total cases of alcohol sold by DLC to licensees. Table 2 shows the sales value and quantity separately for wine, beer cases, and beer kegs. Of note, special orders represents nearly one-half of DLC wholesale revenue from wine products and 38% of the wine cases sold.

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<sup>1</sup> Montgomery County Department of Liquor Control Inventory Management, prepared by Watkins Meegan LLC for the Montgomery County Office of Internal Audit, July 9, 2014. p. 41.

**Table 2. Value and Quantity of FY14 DLC Wholesale Beer and Wine Sales – Stock and Special Order**

Wholesale Sales	Stock Products		Special Order Products	
	Total Sales	# of Cases Sold	Total Sales	# of Cases Sold
Wine	\$26.8 million	384,239	\$23.9 million	234,114
Beer – Cases	\$67.1 million	3.4 million	\$2.8 million	62,684
Beer – Kegs	\$8.2 million	84,234*	\$782,575	5,636*

\*Beer keg quantities refer to the number of kegs sold.

Source: DLC

DLC applies standardized wholesale markups for special order products – 35% for beer cases, 43% or 45% for beer kegs, and 25% (if <\$18 per bottle) or 15% (if \$18+ per bottle) for wine cases. The markup is applied to each product based on DLC’s purchase price, and does not change whether DLC purchased the product from a manufacturer/supplier or from another wholesaler/distributor.

DLC purchases the products it sells from more than 300 sources – alcoholic beverage producers, wholesalers, and retailers. DLC pays the least amount for products purchased directly from producers because those items do not include any wholesale and/or retail markup. Purchasing items from wholesalers or retailers raises prices for DLC (and for subsequent purchasers) because those middlemen incorporate their own mark-up that DLC must pay.

OLO’s analysis of DLC vendor data shows that approximately 81% of all special order products (including liquor) are purchased from other wholesalers or retailers while 15% are purchased directly from producers. In comparison, only 18% of stock products are purchased from other wholesalers/retailers.<sup>2</sup> As a result, many of DLC’s special order products have two wholesale markups incorporated into the overall cost of those products (sometime described to as creating a “fourth tier” in the typical three-tier alcohol distribution system).

## **B. Issues with Special Orders and Stakeholder Feedback on Option 4**

Special orders were a frequent topic of frustration, concern, and complaint from licensees in OLO’s surveys and interviews and from the licensees, distributors and manufacturers who participated in the Ad Hoc Committee’s March 20 worksession. This section briefly summarizes the problems identified with special orders and reviews the written comments the Committee has received from stakeholders specifically related to Option 4.

### **1. Summary of Stakeholder Concerns with DLC Special Orders**

**Insufficient availability of special order products.** Approximately 60% of respondents in both of OLO’s surveys indicated that the availability of special order products through DLC is inadequate for their business needs. Multiple individuals expressed concerns to the Committee about how DLC handles and stores specialty beer and wine products – and reported that some specialty product producers decline to sell their product in the County based on these concerns.

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<sup>2</sup> OLO Report 2015-6, pg. 56.

**Slow and unreliable timing and delivery of special orders.** Approximately 65% of respondents in both of OLO's surveys indicated that the time it takes DLC to deliver special order products is unreasonable. OLO specifically heard from several licensees that they would purchase more special order products if the process for getting those products were quicker. For example, one licensee provided survey feedback stating: "My special orders would be closer to 100% if they didn't take so long to get. I end up having a bad and boring selection of products because the special orders are so inefficient and slow."<sup>3</sup>

**Poor ordering process and customer service.** Over 60% of respondents in both surveys indicated that DLC's ordering process for special order products does not work well for their business. When they order special order products, several licensees report that they do not know when they will receive the products, that the products are delivered in the wrong quantities, and the products do not show up when they are expected because they get "lost" at DLC's warehouse. DLC's new Oracle-based iStore ordering system, used for both stock and special order products, was a specific source of frustration for licensees.

**Pricing/cost of special orders is too high.** In both surveys, over 50% of respondents reported that DLC's wholesale pricing for special order beer and wine products is "high" or "very high." In comparison, respondents were more likely to categorize wholesale pricing for stock products as "reasonable."

## **2. Written Comments on Option 4 from Stakeholders**

In both of OLO's surveys, licensees were asked whether they would favor or oppose various changes to the current structure of liquor control in Maryland and/or Montgomery County. Allowing licensees to purchase special order products directly from private distributors received the most support – 82% of respondents favored that change in the first survey, and 87% of respondents favored that change in the second survey.

In addition to participating in Committee worksessions, several stakeholders submitted written comments to the Committee that specifically addressed Option 4. Included in the table below are:

- Comments received in advance of the Committee's March 20 worksession that were included in the worksession packet (from two licensees and one private wholesaler); and
- Comments sent in after the March 20 worksession (from the County Alcoholic Beverages Advisory Board, one licensee, and four private wholesalers).

The complete text of all the comments summarized in the table are attached beginning at ©1.

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<sup>3</sup> OLO Report 2015-6, pg. 47.

Written Comments on Option 4 published in March 20 <sup>th</sup> worksession packet	
Mike Hill <b>Adega Wine Cellers and Café</b>	I like the idea of privatizing special order items, and leaving the stock items to the County. This seems like each side is giving a little, and this would be a win-win for smaller specialty stores like Adega.
Justin McInerney <b>Capital Beer and Wine</b>	In the short-term, I am strongly in favor of Option 4 of the report "Private Wholesale of Special Order Beer/Wine."
Bob Mutschler <b>Republic National Distributing Company</b>	<ul style="list-style-type: none"> <li>• I'm responding to your request by simply pointing out two areas that directly affect my business in the county and I am not offering any opinions on a direction to go to in the future.</li> <li>• Concerning option #4, private distributors to fill and distribute special orders, would alleviate a major licensee complaint. Assuming that the Maryland Beverage Journal would apply, licensees would have a greater selection of wines, lower prices by eliminating a tier of mark up, quantity deals that might be available and probably credit terms. Special orders are very difficult to manage in the DLC warehouse because when they are received, they have no warehouse location, therefore when pulled to be delivered are difficult to find.</li> </ul>
Written Comments on Option 4 received after March 20 <sup>th</sup> worksession	
Rebecca Ramirez, Chair <b>Montgomery County Alcoholic Beverages Advisory Board</b>	<p>From a public health perspective, here are the questions/concerns I have with Option 4:</p> <ul style="list-style-type: none"> <li>• What mechanisms would be put in place to define what constitutes a special order product? The DLC would need to have oversight of these product lists and the quantities being ordered, so as to preclude almost all beer and wine products from being listed as "special orders."</li> <li>• How will potentially dangerous new products be prevented from being included on a product order list by distributor? In the past, DLC has had the authority to choose not to list products (e.g., Four Loko, jello shots, etc.) that can either be potentially attractive to youth or have dangerous serving sizes or other concerns.</li> <li>• Will the DLC (and by extension the Board of License Commissioners) have the regulatory authority to license, enforce, and if necessary, adjudicate violations by distributors should there be undue influence by private distributors on retailers that prevents a fair, yet competitive, market?</li> </ul> <p>In summary...I have concerns that Option 4 will eventually result in the complete private distribution of alcoholic beverages in Montgomery County.</p>
Johnna Gilchrist <b>Gilly's Craft Beer &amp; Fine Wine</b>	<ul style="list-style-type: none"> <li>• My business is 95% special order...our customers come to us for the newest, most limited and exclusive products available. We have to support the core brand all year long in order to be eligible to get these products. If the distributor could deliver the product in a safe, controlled and timely manner, that would be fantastic. As it is now, with the way the timing in the county works we are about 3 weeks behind the rest of the country on limited release items (it's quite embarrassing). I would happily pay a tax or fee to the county if I was sure that my product would be delivered correctly, on time and intact. Option #4 of the OLO sounds perfect.</li> <li>• In closing, the revenue from the DLC each year goes towards some good things in the county. I realize this. I would be in support of option #4 to start. It would be the best scenario, for the group of licensees who seem to really be having the most trouble with the DLC in its current state.</li> </ul>

<p><b>Licensed Beverage Distributors of Maryland, Inc.</b></p> <p>James Smith Kevin Dunn <b>Reliable-Churchill LLP</b></p> <p>Joel Polichene Thomas White <b>Republic National Distributing Company</b></p>	<ul style="list-style-type: none"> <li>• Under Option 4, a wholesaler would have to make a special trip to the licensee making a special order. Simple economics makes this impractical and impossible. The expense of diverting a driver and truck to a distant location for the delivery of a special order, which by its nature is a small order such as a case of wine, far exceeds the profit of such a delivery. A wholesaler could not charge a special delivery fee in Montgomery County because it has to charge all Maryland licensees the same price for the product and delivery no matter the location of the licensee. (There is a minimum order requirement for regular customers, but it would not cover the expense of a special order delivery in Montgomery County.)</li> <li>• Having wholesalers make the special order deliveries also would not necessarily eliminate wait time...If there is a lag time in the final step of the process, it could be solved by the licensee picking up the product from the Department or the creation of a special order delivery vehicle at the Department which would make deliveries the day the product arrives at the Department.</li> <li>• Option 4 will not work for a simple reason: wholesalers are not required to make a money losing delivery simply because an order is placed. Wholesalers most likely would not deliver a special order because they would lose money. In short, Option 4 is not the solution to the special order issue in the County.</li> </ul>
<p>Matthew Tucker <b>The Country Vintner</b></p>	<ul style="list-style-type: none"> <li>• Contrary to assertions made by the Licensed Beverage Distributors of Maryland, Option 4 is economically viable and there would be no extraordinary financial burden associated with making special order deliveries directly to retailers in Montgomery County, just as deliveries are made direct to retailers in the ordinary course in every other locality in the State.</li> <li>• If adopted, Option 4 would be beneficial to Montgomery County because it would remove a labor intensive and burdensome line of distribution from the County and would give TCV direct access to retail licensees, which in turn would provide greater access to a variety of products and increased ability to compete within the regional market.</li> <li>• The ability of wholesalers to make the special order deliveries would make products available to retail licensees and ultimate consumers much more quickly and efficiently since the licensee would not have to wait for the DLC to deliver the special order as part of its regularly-scheduled delivery.</li> <li>• Implementing Option 4 would provide DLC with an increased opportunity to focus on and implement other strategies to help ensure the long-term success of its remaining operations.</li> </ul>
<p>Erin Tyler, <b>Legends Limited</b></p>	<ul style="list-style-type: none"> <li>• Distributing and storing beer properly is different than distributing wine or spirits. Wine and spirits have a much longer shelf life, does not require cold storage, does not incur a large seasonal or special release packages and does not have the high rate or rotation of tap line in bars or package placements at retail. This presents special issues for the Montgomery County Department of Liquor Control and Legends. Legends has had difficulty in the past with our special order stock going out of code in the DLC's warehouse, abiding to proper credit terms and getting delivery to the retailer in a timely manner.</li> <li>• Under Option 4, wholesalers such as Legends would deliver special orders directly to the licensee. Option 4 could be economically viable. It may be worth the investment by Legends to invest in an additional truck and personnel to make special order deliveries directly to retailers in Montgomery County, just as deliveries are made direct to retailers in the ordinary course in every other locality in the state. This option would allow better control of our products and further guarantee a timely delivery for our customer in the county.</li> </ul>

### C. Implementing Option 4

This memo describes two potential implementation methods for Option 4:

<b>"Open Distribution" Method</b>	Require <u>or</u> allow private wholesale ordering, processing, and delivery of special order beer and wine products
<b>"Drop Ship" Method</b>	Maintain County ordering and processing while requiring <u>or</u> allowing private wholesale delivery of special order beer and wine products

In addition, as part of its Operational and Business Action Plan, DLC currently is analyzing a third method for solving problems associated with special orders: enhancing internal effectiveness and efficiency within the current structure. DLC plans to provide details on this "Internal Improvement" approach when it updates the Committee on its Action Plan.

This section provides detail on both the open distribution and drop ship methods, identifies various implementation issues/questions associated with each, discusses ways to implement changes, and analyzes the extent to which the methods would address the problems identified with the current special order process for beer and wine.

#### 1. Open Distribution Method

Open distribution would privatize all aspects of the special order beer and wine wholesale distribution process in Montgomery County. Specifically, private Maryland licensed wholesalers would control the sale and distribution of special order beer and wine products – including ordering, processing, billing/payment, delivery, returns, disbursement of excise taxes to the State, etc. – as they do in other Maryland counties.

The County could require wholesalers to participate in open distribution (i.e., private wholesalers would have to distribute special order products for that product to be available in Montgomery County) or could give wholesalers the option to participate (i.e., private wholesalers would choose whether to self-distribute their special order products or whether to continue to provide their products through DLC as the wholesaler). Providing private wholesalers the option to participate in an open distribution system (rather than requiring participation) would provide the most flexibility for wholesalers.

The open distribution method would model the changes made to the State law (effective July 1, 2014) that give certain small breweries and wineries the option to self-distribute products directly to Montgomery County licensees instead of going through DLC. Since that law has gone into effect, some small breweries have chosen to self-distribute, while others have chosen to continue distribution through DLC.



**a. Open Distribution – Defining "Special Order"**

Allowing private wholesalers to sell and distribute special order items requires criteria for designating products as special order vs. stock. OLO recommends giving DLC the authority to control the designation of items as stock vs. special order, or otherwise creating a specific threshold or standard to designate products. The alternative – giving private wholesalers control of the designation – could result in a de facto deregulation of the entire system if wholesalers designated all of their products as special order.

The Committee could endorse one of several approaches to designating items as stock vs. special order, such as:

- Giving DLC authority to designate items as stock or special order once or twice a year, with the option to change items from one designation to the other at that time (and designating new items as stock or special order when they are listed for sale).
- Basing the designation of stock or special order on the amount of a product sold in the County (either by volume or number of cases/kegs sold) – products that exceed a threshold of cases or volume sold the prior year would be designated as stock items and products below the threshold would be special order.
- Freezing DLC's stock order list as it currently exists, and listing all other items as special order (including all new items added in the future).

OLO recommends the first approach, giving DLC authority to periodically determine whether items are stock or special order. Internally, DLC should establish clear criteria and standards for designating items as stock or special order. If DLC designates an item as stock, it should be expected that the item is typically available for a licensee's next scheduled delivery when ordered except in unusual or extraordinary circumstances. Additionally, DLC should establish performance criteria for delivery of stock items. If DLC cannot meet those criteria, the item should then be moved to special order status.

Private wholesalers may express concern that, over time, DLC could re-classify popular and profitable special order products as stock items. DLC, however, always will be limited in making such changes by the capacity of its warehouse. Additionally, as detailed in OLO's report, DLC staff report that when they have moved high-demand special order items to stock status in the past, sales often slowed considerably and DLC re-designated the products as special order.<sup>4</sup> To address this in a clear and transparent manner, the Council could require that DLC develop specific criteria that would have to be met before a special order product could be switched to stock.

Under this model, DLC would also maintain its current process for approving a product for sale in Montgomery County and thus retain the ability to prevent dangerous products from being sold.

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<sup>4</sup> OLO Report 2015-6, pg. 19.

**b. Open Distribution – What if a supplier refuses to sell a product in Montgomery County unless it is special order?**

Keeping the stock or special order distinction under the control of DLC would address any issue of a supplier refusing to sell a product in Montgomery County unless the product was designated as special order. If a company did not agree with DLC's categorization of their product as stock or special order, they could choose not to sell their product in Montgomery County – just as they can do under the existing structure.

Currently, an alcohol supplier or producer can decide not to sell their product via the DLC in Montgomery County (forgoing any sales revenue for the product) even if they distribute through private wholesalers in other areas of Maryland. Some speakers at the Committee's March 20 worksession, as well as some stakeholders that have submitted written correspondence, indicated that in their experience some producers do not sell their products in Montgomery County because of the County's distribution structure and practices.

Under Option 4, many suppliers may want a product categorized as special order so they can use their existing private wholesalers for distribution instead of the DLC. It is unlikely, however, that a company currently selling stock products to DLC (and presumably making a profit) would choose to remove itself from the Montgomery County market entirely (and forgo its current profit) if DLC refused to change a product categorization to special order.

**c. Open Distribution – Economic Viability for Private Wholesalers**

Whether an open distribution system for special order beer and wine would be economically viable for private wholesalers is a question for individual wholesalers. Accordingly, OLO suggests that participation in an open distribution system be optional for wholesalers, allowing each wholesaler to determine whether it makes sense for their business to distribute special order products to retail licensees or to continue to sell products directly to DLC. The intent behind an open distribution model is not to force any private wholesaler to participate in a potentially unprofitable system.

If participation in an open distribution system is optional for private wholesalers, OLO recommends requiring a private wholesaler to declare – via a distribution permit or some other formal mechanism – if it will distribute special order products directly to Montgomery County licensees. If it chooses to do so, the private wholesaler would be responsible for all aspects of distributing special order products it is licensed to sell in the State of Maryland. Additionally, a wholesaler would have to charge Montgomery County licensees the same price as it charges in the rest of the state for each product. Any stock products or liquor products purchased from that same wholesaler would still be distributed through DLC.

Alternatively, the County could allow retail licensees to choose whether to order a special order product through DLC or the private wholesaler. While providing greater flexibility for the licensee, OLO believes this approach would have a greater potential for confusion and mistakes (as well as more work from a coordination, logistical, and record-keeping perspective) if two different wholesalers (DLC and a private company) had the authority to distribute the same product in the County.

Many private Maryland wholesalers have minimum order requirements, requiring purchasers to order a minimum dollar amount (e.g., \$150) or a minimum number of cases (e.g., 3 cases or more) in any given order – presumably to ensure that an order is economically beneficial to the wholesaler. OLO recommends ensuring that private wholesalers retain the ability to set and/or maintain minimum order requirements for orders by Montgomery County licensees should the County institute an open distribution system for special order beer and wine.

As noted previously on page 6, the Ad Hoc Committee has received formal correspondence from four private distributors that comment on the potential economic viability of Option 4. Two of the distributors, The Country Vintner and Legends Limited, indicated that it would be economically viable; while the other two other distributors, Reliable Churchill and Republic National Distributing Company (writing jointly as the Licensed Beverage Distributors of Maryland, Inc.) indicated that it would not.

**d. Open Distribution – Implementation Schedule**

The open distribution method would require changes to state law. The earliest a potential bill could be introduced in the General Assembly would be the next legislative session beginning January 2016. If a bill were passed by the General Assembly and signed by the Governor in the next session, the earliest it could take effect would likely be FY17.

**e. Open Distribution – Addressing Concerns Identified with Special Orders**

As evidenced by OLO's surveys as well as feedback provided at Ad Hoc Committee worksessions, there is strong support for Option 4 among licensees. The open distribution method could address the concerns about special orders detailed on pages 3-4 as follows:

**Product Availability.** Beer and wine manufacturers that currently do not sell their products in Montgomery County because of concerns about DLC would be more likely to distribute their product in the County via private wholesalers that sell their products throughout the rest of the State and/or region.

**Timing and Delivery.** Wholesalers could deliver products directly to licensees without the product having to go first to DLC and then wait until DLC's next scheduled delivery date for that licensee. Eliminating this extra step would get special order products to licensees more quickly.

**Ordering and Customer Service.** Private wholesalers employ sales representatives who are familiar with the products they sell and, presumably, could provide a higher level of service to Montgomery County licensees as they have a stronger incentive than DLC to maintain or increase sales of their particular products. Additionally, licensees could order special order products directly through private wholesalers instead of through DLC's iStore system.

**Price and Cost.** An open distribution system should reduce the price of products for licensees for most or all special order products DLC currently purchases from another wholesaler. Purchasing directly from a private wholesaler would eliminate DLC's markup (ranging from 15% to 45% depending on the product).

**f. Open Distribution – Impact on County Jobs**

In Report 2015-6, OLO estimated that implementing Option 4 could lead to a reduction of up to 15 positions in DLC. This estimate assumed all special order beer and wine products would be distributed privately. If the County implemented an optional open distribution system for special order beer and wine, the actual impact on DLC positions would likely be smaller depending on the level of private wholesaler participation. It is likely that any position reductions resulting from implementation of Option 4 could occur via natural attrition. Additionally, DLC intends to open three new stores in the near future, adding approximately 22 retail positions. These added positions would more than offset any positions eliminated due to implementation of Option 4.

**2. Drop Ship Method**

The drop ship method would require or allow private wholesalers to deliver special order beer and wine products directly to licensees in Montgomery County, while DLC maintains responsibility for all ordering, processing, and billing/payment functions. Once DLC received and processed a special order, a private wholesaler could then deliver the product directly to a licensee's place of business.

Similar to open distribution, the County could require private wholesalers to participate in a drop ship system (i.e., private wholesalers would be required to deliver all special order products directly to licensees) or could give private wholesalers an option to participate (i.e., private wholesalers could choose whether to deliver special orders directly to licensees or continue to deliver them through DLC).

Because different wholesalers may have different views on the economic benefit of Option 4 to their specific business model, the more reasonable and flexible approach is to make this provision optional to wholesalers – giving them the opportunity to decide for themselves whether delivering special order products makes sense for their businesses. DLC likely would substantially reduce (but still charge) its markup on special order products delivered via drop ship because DLC delivery costs would be reduced.

DLC currently is seeking feedback from the State Comptroller's Office on the legality of the drop ship method under current state law. At issue is the "come to rest" provision of State law, which requires that "[b]efore any sale and delivery to a retail licensee, any alcoholic beverages acquired by a wholesaler from any source shall first come to rest on the licensed premises of the wholesaler."<sup>5</sup> If the Comptroller's Office determines that the drop ship method is not legal under current law, implementing a drop ship system would also require changes to State law.

**a. Drop Ship – Defining "Special Order"**

Under the drop ship method, DLC would maintain its current process and structure for categorizing products as stock or special order, as well as approving products for sale. The only change would be that private wholesalers could deliver special order products directly to a licensee instead of to DLC's warehouse.

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<sup>5</sup> Md. Code, Article 2B, §2-301F(2)

**b. Drop Ship – What if a supplier refuses to sell a product in Montgomery County unless it is special order?**

As with the open distribution method, keeping the stock or special order distinction under the control of DLC would address any issue of a supplier refusing to sell a product in Montgomery County unless the product was designated as special order. If a company did not agree with DLC's categorization of their product as stock or special order, they could choose not to sell their product in Montgomery County – just as they can do under the existing structure. OLO believes it is unlikely that suppliers would remove products currently for sale in Montgomery County as stock items (and thus give up current profits) merely to control the means of delivery.

**c. Drop Ship – Economic Viability for Private Wholesalers**

As with open distribution, whether a drop ship system for special order beer and wine would be economically viable for private wholesalers is a question for those businesses. Accordingly, OLO suggests that participation in a drop ship system be optional for wholesalers because the intent behind this potential change is not to force a private wholesaler to participate in a system that a wholesaler may consider unprofitable.

As with open distribution, DLC could require a private wholesaler to declare – via a delivery permit or some other formal mechanism – if it will deliver special order products directly to Montgomery County licensees. If it chooses to do so, the private wholesaler would be responsible for all aspects of delivering products once an order is received from DLC. Any stock products or liquor products from that same wholesaler would still be distributed through DLC.

The formal correspondence from distributors (summarized on pages 5-6) did not directly address the drop ship method as compared to the open distribution method as this idea was presented after publication of OLO Report 2015-6.

A drop ship system raises a somewhat different question of economic viability than the open distribution method. Specifically, whether allowing private wholesalers to deliver special order products without also allowing them to manage the other parts of the distribution process would provide enough benefits to be worthwhile (i.e., profitable) for the wholesaler. Private wholesalers would likely accrue additional costs to make deliveries and would need to increase prices or increase sales volume to achieve commensurate economic benefits.

Because private wholesalers are set up to manage the entire distribution process as opposed to just the delivery process, it is not clear whether the drop ship method would provide enough economic efficiencies over the current structure for private wholesalers to participate.

**d. Drop Ship – Implementation Schedule**

One advantage to the drop ship method is that it potentially could be implemented in FY16 if the State Comptroller determines it does not require a change in State law. If not, the implementation schedule would mirror that of the open distribution method – the earliest a State law change could be introduced would be January 2016 and the earliest implementation would likely be in FY17.

**e. Drop Ship – Addressing Concerns Identified with Special Orders**

As evidenced by OLO's surveys and feedback provided at Committee worksessions, there is strong support for Option 4 among licensees. The drop ship method would address many of the identified special order issues, but in some cases to a lesser extent than the open distribution method.

**Product Availability.** Beer and wine manufactures that currently do not make their product available in Montgomery County because they do not believe DLC would handle their product in their preferred manner would be more likely to distribute their product via private wholesalers who also handle their product throughout the rest of the State. However, private wholesalers may be less likely to participate under the drop ship method because they would control only delivery.

**Timing and Delivery.** Wholesalers could deliver products directly to licensees without the product having to go first to DLC and then wait until DLC's next scheduled delivery date for that licensee. Eliminating this extra step would get special order products to the licensees more quickly.

**Ordering and Customer Service.** Private wholesalers employ sales representatives who are familiar with the products they sell and, presumably, could provide a higher level of service to Montgomery County licensees because they have a stronger incentive than DLC to maintain or increase sales of their particular products. However, licensees would still have to use DLC's Oracle system to order special order products. Additionally, the drop ship could create new customer service issues or confusion by separating the billing and payment functions from the delivery and return functions.

**Price and Cost.** Retail licensees' wholesale costs for special order wine and beer would likely decrease if DLC lowered its markup for special order products delivered by private wholesalers under the drop ship method.

**f. Drop Ship – Impact on County Jobs**

In Report 2015-6, OLO estimated that implementing Option 4 could lead to a reduction of up to 15 positions in DLC. This estimate assumed all special order beer and wine products would be distributed privately. Under the drop ship method the actual impact on DLC positions would likely be smaller depending on the level of private wholesaler participation. It is likely that any position reductions resulting from implementation of Option 4 could occur via natural attrition. Additionally, DLC intends to open three new stores in the near future, adding approximately 22 retail positions. These added positions would more than offset any positions eliminated due to implementation of Option 4.

**D. Alternative Revenue Generation**

Allowing the private wholesale distribution of special order beer and wine would reduce County profit from the sale of these products. This section describes ways to replace some or all of the lost revenue by charging fees to distributors for the ability to sell alcohol directly to retail licensees in Montgomery County. State law prohibits local jurisdictions from taxing the sale of alcoholic beverages, so the methods for revenue generation are fee-based, not tax-based. Each method would require changes to State law to authorize the County to institute the fees.

### 1. Annual Gross Profit from Special Order Beer and Wine Sales - \$5-\$7 million annually

Between FY12 and FY14, the sale of special order beer and wine generated approximately 20% of DLC's wholesale revenue annually and 10% of DLC's total revenue. As part of the budgetary/fiscal impact for Option 4 included in OLO Report 2015-6, OLO estimated a potential loss of gross profit from DLC special order beer and wine of \$5-\$7 million per year. OLO developed this estimate using data on FY14 sales and DLC's special order markups, shown in the table below.

**Table 3. Estimated Gross Profit from DLC FY14 Wholesales Special Order Beer/Wine Sales**

Wholesale Sales	Wine	Beer – Cases	Beer – Kegs	Total
Total Sales	\$23.9 million	\$2.8 million	\$782,575	\$27.5 million
DLC Markup	15% - 25%	35%	43% - 45%	--
Est. Gross Profit (sales x markup)	\$3.6-\$6.0 million	\$980K	\$337K-\$352K	\$4.9-\$7.4 million

**How much revenue might DLC lose under Option 4?** While DLC's total estimated gross profit is \$5-\$7 million for special order beer and wine, it is unlikely that DLC would lose the entire amount. Factors that would impact how much profit DLC might lose if Option 4 were implemented include:

- **Implementation Method.** The open distribution method provides the most "risk" to current DLC profit from special orders because DLC would no longer receive any revenue for special order products distributed by private wholesalers. Under the drop ship method, DLC would still be able to charge a markup but it would likely be much lower. For example, if DLC charged a flat 5% markup for all special order products the gross profit in FY14 would have been approximately \$1.4 million.
- **Participation by Private Wholesalers.** As detailed in the correspondence to the Ad Hoc Committee, some private wholesalers believe Option 4 is economically viable for their business model while others do not. As a result, if given the option, some private wholesalers may not participate (under either implementation method). DLC would maintain the revenue from any special order products that continue to go through DLC's wholesale operations. For example, if only one-half of special order beer and wine products switched to private wholesale, the potential gross profit loss may also decrease by half, to \$2.5-\$3.5 million.
- **Potential Revenue Offsets.** DLC's FY16 approved operating budget includes plans to open three new retail stores. According to DLC's Long-Range Strategic Plan document, its retail stores produce a net annual income of approximately \$800,000 on average. As a result, once these new stores are up and running, DLC may achieve an additional \$2.4 million in annual profits that offsets some or all of the lost revenue from Option 4.

## 2. Replacing Lost Revenue

This section describes two methods for generating revenue based on fees on private wholesalers selling special order beer and wine products in the County. The first method would generate revenue based on the volume of alcohol that private wholesalers distribute in the County. The second method would generate revenue based on required fees for registering products for sale in the County.

### a. Volume-Based Distribution Fee

A volume-based distribution fee – a per unit fee for alcohol sold in the County – would require wholesalers to pay a fee based on the amount of alcohol distributed to licensees in the County. To estimate potential revenue from a volume-based distribution fee, OLO used DLC data on the number of cases and/or kegs of special order beer and wine sold by DLC's wholesale division in FY14.<sup>6</sup> Table 4 estimates revenue using three variations for assessing a distribution fee based on the amount of alcohol sold by a private wholesaler. The methods are:

- **Flat fee per ounce of alcohol distributed in the County.** A flat per ounce distribution fee would generate an estimated \$1 million for every 1¢ of the fee. A 1¢ fee equates to about 72¢ per six-pack of beer and 25¢ per 750 mL bottle of wine.
- **Variable fee per ounce of alcohol distributed in the County.** A variable per ounce distribution fee that charges three times as much for wine (3¢ per ounce) as for beer (1¢ per ounce) – similar in concept to the State's alcohol excise tax structure – would generate an estimated \$2.4 million. A 3¢ fee for wine equates to about 75¢ per 750 mL bottle.
- **Per-case or per-keg fee, varying by the type of alcohol sold.** A per case distribution fee was suggested by a licensee who participated in OLO's survey. A variable fee of \$3 per case of beer, \$5 per case of wine, and \$20 per keg (a ½ keg of beer is equivalent to a little over six cases) would generate an estimated \$1.5 million.

The revenue estimates shown in the next table are based on the specified fee increment and can be adjusted up or down to achieve a different revenue level. Additionally, if implementing Option 4 (under either the open distribution method or the drop ship method) led to increased purchases of special order products by licensees and/or recapturing of cross-border sales, the total fee-based revenue would increase (perhaps significantly based on the estimated value of cross-border sales).

**Table 4. Estimated Revenue from a Fee on the Private Wholesale Distribution of Alcohol**

Method	Revenue from Beer	Revenue from Wine	Total Revenue
1¢ per ounce of alcohol	\$292,000	\$714,000	\$1.0 million
1¢ per ounce of beer, 3¢ per ounce of wine	\$292,000	\$2.1 million	\$2.4 million
\$3 per case of beer, \$5 per case of wine, \$20 per keg	\$301,000	\$1.2 million	\$1.5 million

<sup>6</sup> For estimation purposes, OLO assumed all cases of beer were 12 ounce cans/bottles (288 ounces per case); all cases of wine were 750 mL bottles (304.8 ounces per case); and all kegs were ½ keg size (1,984 ounces per keg). A portion of DLC's actual special order wholesale sales in FY14 are for different sized cases or kegs.



## b. Brand Label Registration Fee

A product-based registration fee would require private wholesalers to register each product that they want to sell in the County. Many states require alcohol producers, wholesalers, and/or importers to register the products that they sell in a state and charge a registration fee— typically referred to as “brand registration” or “brand label registration”. Some states require a one-time registration fee while other states require an annual registration fee. The table below summarizes the brand registration fees in certain states.

**Table 5. Summary of Some State Brand Label Registration Fees**

State	Fee
<b>Annual or Semi-Annual Fee</b>	
Florida	Beer – \$30 per label annually Wine – \$15 per label annually Liquor – \$30 per label annually
Minnesota	\$40 per label for initial registration good for three years, \$30 per label renewal fee
New York	\$50 per label annually
Tennessee	Beer – \$100 per label annually Wine – \$250 per label annually Liquor – \$250 per label annually
<b>One-Time Fee</b>	
Connecticut	\$200 per label (\$15 per label for products manufactured in CT by a CT manufacturer)
New Jersey	\$23 per product
South Dakota	Beer – \$25 per label Wine – \$25 per label (\$17.50 per label after the first label) Liquor – \$50 per label
Virginia	\$30 per label

Source: State online codes and tax records

OLO Report 2015-6 estimated the potential revenue from a flat \$1,000 product registration fee for all DLC stock and special order products. This section applies a potential registration fee to special order products only, and uses a lower per product fee similar to the state fees shown above. As of March 2015, DLC lists 3,393 special order beer products and 20,136 special order wine products for wholesale purchase. Table 6 estimates revenue from brand label registration at different fee levels, assuming all special order beer and wine products are registered.

**Table 6. Estimated Revenue from a Brand Label Registration Fee**

Method	Revenue from Beer	Revenue from Wine	Total Revenue
Flat Fee – \$30 per brand (same as Virginia)	\$102,000	\$609,000	<b>\$711,000</b>
Flat Fee – \$50 per brand	\$170,000	\$1.0 million	<b>\$1.2 million</b>
Variable Fee – \$50 per beer, \$100 per wine	\$170,000	\$2.0 million	<b>\$2.2 million</b>

The total revenue estimated for each method in Table 6 could be increased or decreased by adjusting the amount of the fee. Additionally, if implementing Option 4 (under either the open distribution method or the drop ship method) increased the amount of special order products made available for sale in the County, the total revenue for each method would increase.

### **3. Impact of Distribution Fees on the Wholesale Price of Alcohol in Montgomery County**

One concern raised about enacting a distribution fee on special order products under Option 4 is that, depending on the fee structure, it would raise overall alcohol prices when high prices for special orders are already a frequent complaint among licensees. Instituting a wholesale fee on private distributors in Montgomery County that differs from other Maryland counties may provide an incentive for distributors to raise the wholesale price of products for Montgomery County businesses. Current state law, however, requires distributors to charge all customers the same price for products, which would prevent distributors from increasing prices only in Montgomery County.

**Additionally, eliminating the DLC markup on special orders distributed by private wholesalers could mitigate the cost impact of a distribution fee.** This would be particularly true for special order products that DLC purchases from other wholesalers that have two wholesale markups incorporated into the price that licensees pay. Examples of the cost impact from a distribution fee compared to DLC's markup for special order beer and wine cases are shown below, based on the fee increments used in Table 4.

- **Beer case (consisting of 24 12-ounce bottles/cans).** A distribution fee of 1¢ per ounce would add \$2.88 per case or 72¢ per six pack of beer. In comparison, DLC's 35% markup for the top selling special order beer case in FY14 adds \$9.12 per case or \$2.28 per six pack (calculation based on DLC's wholesale price of \$35.30 per case for this product minus the 20¢ in State excise taxes included in the wholesale price).
- **Wine case (consisting of 12 750-mL bottles).** A distribution fee of 1¢ per ounce would add \$3.04 per case or about 25¢ per bottle, and a fee of 3¢ per ounce would add \$9.14 per case or about 76¢ per bottle. In comparison, DLC's 25% markup for a top-5 selling special order wine case in FY14 adds \$13.71 per case or \$1.14 per bottle (calculation based on DLC's wholesale price of \$69.48 per case for this product minus the 95¢ in State excise taxes included in the wholesale price).

### List of Attachments

Written Comments from:	Begins at:
Mike Hill, <i>Adega Wine Cellers and Café</i> , March 14, 2015	©1
Justin McNerny, <i>Capital Beer and Wine</i> , February 26, 2015	©3
Bob Mutschler, <i>Republic National Distributing Company</i> , March 17, 2015	©5
Rebecca Ramirez, Chair, <i>Montgomery County Alcoholic Beverages Advisory Board</i> , March 26, 2015	©6
Johnna Gilchrist, <i>Gilly's Craft Beer &amp; Fine Wine</i> , March 25, 2015	©9
<i>Licensed Beverage Distributors of Maryland, Inc.</i> , March 19, 2015 James Smith and Kevin Dunn, <i>Reliable-Churchill LLP</i> Joel Polichene and Thomas White, <i>Republic National Distributing Company</i>	©11
Matthew Tucker, <i>The Country Vintner</i> , May 4, 2015	©15
Erin Tyler, <i>Legends Limited</i> , May 28, 2015	©19

Hill  
Adega Wine Cellars/Cafe

**Subject:** FW: Liquor Control Meeting on Friday, March 20

**From:** Michael Hill [mailto:mike@adegawinecellars.com]  
**Sent:** Saturday, March 14, 2015 6:09 PM  
**To:** Heyboer, Tommy  
**Subject:** Re: Liquor Control Meeting on Friday, March 20

Good afternoon Tommy. Thank you for taking my feedback into consideration, and thank you for making such significant progress in attempting to improve a very broken and flawed system. I look forward to seeing you on Friday.

To answer your questions:

1. What is your current relationship with the Montgomery County DLC? What kind of business do you do with them?

*We are a cafe/retailer licensee through the county. We purchase beer and wine with roughly 85%-90% of our items purchased being special order.*

2. What is your experience like working with the DLC? What challenges do you face? If applicable, what are the differences you see between doing business with the DLC and doing business with private distributors in other jurisdictions? Do you think the DLC makes it easier, harder, or neutral for you to do business in the County?

*My experience with the DLC has been mostly poor. My greatest challenges are consistent errors with my deliveries, and a lack of communication as to why they consistently drop the ball. The inability for the DLC to deliver items that our loyal customers wait weeks upon weeks for greatly affects our top line. The inconsistencies (3 cases of XYZ wine ordered, 7 cases delivered; 5 cases of 123 wine ordered, 11 bottles delivered!!!) are a major issue.*

*I had a much easier time as a buyer for a DC restaurant. I even had a much easier time as a buyer in the heart of the bible belt in Atlanta, GA, where I lived for 6 years!!! As a customer, I hate to admit it, but it's much easier buying alcoholic beverages in DC and P.G. County due to lower prices and better selection.*

*The DLC definitely makes it more difficult for me as I have to explain to my customers why certain items continue to be out of stock, etc. Again, top line revenue is directly affected.*

*One good note, the delivery drivers have improved dramatically ever since the 'Beer Bust' report!*

3. The Committee is considering, at least, five different reform proposals for the DLC. You can view them here: <http://www.montgomerycountymd.gov/COUNCIL/Resources/Files/AdHocComm/DLCReportSummary.pdf> What do you think of each option? Which option would you most prefer? Least prefer?

1. I would fully support a complete deregulation. I realize that this will create a drastic drop in tax revenue collected by the county and the loss of hundreds of union-backed jobs, so Leggett will want nothing to do with this option!
2. Option 2 is a good one. Public safety concerns will diminish if the county still has control of off-premise liquor sales. This will also counter the myth that 'A liquor store will be on every block'...
3. Since we are beer/wine only, I have no preference whether liquor is privatized or not.
4. I like the idea of privatizing special order items, and leaving the stock items to the county. This seems like each side is giving a little, and this would be a win-win for smaller specialty stores like Adega
5. Giving the DLC even more resources to 'function more efficiently' is easily the worst option of the five! The county needs to get out of the alcohol business!

4. The Committee has discussed Option 4 (allowing private distributors to fill and deliver "special orders") at some length. What do you think about Option 4? What would the Committee need to consider to make this option work well for you?

*I think option 4 will work. I would be curious as to whether the County Liquor stores would also be able to carry special order items in addition to their normal stock? The two closest county stores have a significant special order craft beer selection, in addition to some special order wines. How would privatization affect the county stores' inventories?*

5. Broadly, the Committee would like to discuss how alcohol distribution affects the County's economy and quality of life. From your perspective, what, if any, is the relationship between these?

*Most licencees exercise best practices to avoid serving minors and those intoxicated already. I can't imagine anything less than zero tolerance if the county moves towards privatization. Alcohol distribution is a major tax revenue generator for the county, but I can only imagine that the revenue loss from the elimination of 'junk fees' will be offset by the gain due to increased spending due to increased item availability. I for one will spend less in surrounding counties and DC, and keep my money in the county if we move towards privatization.*

*As far as quality of life is concerned, I don't see that being affected. I don't anticipate an increase in alcoholism, or alcohol-related illness. I don't anticipate an increase in alcohol related fatalities. I don't think the two have any correlation.*

Thank you for your time,

MH

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Mike Hill  
Adega Wine Cellars & Cafe  
Store Manager  
8519 Fenton Street  
Silver Spring, Md 20910  
301.608.2200  
301.608.8900(f)

On Thu, Mar 12, 2015 at 12:08 PM, Heyboer, Tommy <[Tommy.Heyboer@montgomerycountymd.gov](mailto:Tommy.Heyboer@montgomerycountymd.gov)> wrote:

Hi Mike —

Thank you for being willing to share your experience with the Montgomery County Liquor Control Committee. In anticipation of the worksession next week, I wanted to share some information with you.

First, the logistics of the worksession are as follows:

Time/Date: 9:30am, Friday, March 20, 2015

Location: Council Office Building  
3<sup>rd</sup> Floor Hearing Room

100 Maryland Ave.

Rockville, MD 20850

McInerney  
Capital Beer & Wine

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**Subject:** FW: comments for Ad Hoc Committee on Liquor Control

**From:** [justin@capitalbeerwine.com](mailto:justin@capitalbeerwine.com) [mailto:[justin@capitalbeerwine.com](mailto:justin@capitalbeerwine.com)]

**Sent:** Thursday, February 26, 2015 9:54 AM

**To:** Riemer Hans

**Cc:** Heyboer, Tommy

**Subject:** comments for Ad Hoc Committee on Liquor Control

Dear Councilmember Riemer,

Thank you for asking me to contribute to the Council's Ad Hoc Committee on Liquor Control. The Department of Liquor Control (DLC) is a monopoly. My thoughts are best summed up Article 41 of the Maryland Declaration of Rights:

"monopolies are odious, contrary to the spirit of a free government and the principles of commerce, and ought not to be suffered."

I have read the Office of Legislative Oversight's report (the Report) as well as the plan commissioned by the DLC. In the short term, I am strongly in favor of Option 4 of the Report "Private Wholesale of Special Order Beer/Wine". In the long term, I am in favor of Option 1 "Full Deregulation".

I have lived most of my life in Montgomery County where it has been legal for me to consume and purchase beer and wine since my eighteenth birthday in 1980. Although I am a lawyer, I am also a beer and wine merchant. First as a consumer and now as a merchant, I have found Montgomery County's alcoholic beverage regulatory structure to be both anti-consumer and anti-business. As a consumer, I rarely shopped for beer and wine in Montgomery County unless I was very short on time. In most instances I would shop at retailers in nearby jurisdictions, typically Northwest, DC. Now as a merchant, I am wholly frustrated by the shortcomings of a dysfunctional, unnecessarily cumbersome system which does not need to exist.

The Report is comprehensive and satisfactorily calls attention to practically all of my concerns with the DLC. This e-mail is only meant to highlight a few points from my view as a retailer.

**DLC stores practice predatory pricing** - A predatory price is a price that is "profit maximizing only because of its exclusionary or other anticompetitive effects". The DLC stores' standard retail wine prices are 28% over wholesale. This is a 21.88% margin which is unsustainable by the average retailer. The DLC stores regularly put wines on sale which yield a 15% margin. Again, this margin is unsustainable by an average retailer. The DLC stores' wine prices are so low that I, and many of my fellow retailers, will carry few, if any, of the same products which the DLC stores carry. This is because a customer will easily note that our prices are significantly higher than the DLC's prices for the same products. As a specialty retailer, my focus is on brands which are not widely available. Nevertheless, many customers still want to purchase some recognizable


brands such as Kendall Jackson. However, I scrupulously avoid carrying brands such as Kendall Jackson because I do not want to look like I am price gouging at my normal mark up. The DLC's retail wine pricing practices effectively exclude national brands from my shelves. This is brazenly anti-competitive and if this were the practice of a private sector retailer, then it would likely be seen as a violation of state and Federal anti-trust laws.

**Many items listed as special order are not available** – This is a small point but I want to note that the Report states that roughly 85% of the DLC's products are special order. Just to clarify, the list of products in the DLC's system is enormous. The fact that a product is listed in the DLC's system only means that the product was at one point available. Many products come and go quickly with the season, market demand, production limits and other factors. The DLC periodically purges its system of the unavailable/discontinued products but it is a never ending process due to the nature of the alcoholic beverages business. Hence, a significant percentage of products which are listed in the DLC's system are not available and will never again be available. Likewise, a significant percentage of products listed in the DLC's system might only be unavailable for a few months or a few weeks until the supply is replenished depending on various factors such as manufacturer's production schedules and the time of year.

In closing, my remarks could go on at length and I hope to engage with the Council further. Thank you for considering my comments. I look forward to continuing this dialogue and participating in the process of addressing the Report's proposals.

Sincerely,



Justin McInerney  
Capital Beer & Wine  
7903 Norfolk Ave.  
Bethesda, MD 20814  
store (301) 656-8855  
cell (301) 300-8947  
 follow me on twitter

Mutschler  
Republic National  
Distributing Company

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**From:** Mutschler, Bob <Bob.Mutschler@RNDC-USA.COM>  
**Sent:** Tuesday, March 17, 2015 10:31 AM  
**To:** Ferber, Justina  
**Subject:** RE: March 20th Meeting

Justina,

Unfortunately, I can't be part of your panel, but I would like to offer some opinions based upon my everyday experiences working with the DLC..

I've worked close to 20 years in MoCo representing as a broker wine, beer and spirits. My company also is a supplier of primarily special order wines totaling about \$4,000,000 annually. I'm responding to your request by simply pointing out two areas that directly affect my business in the county and I am not offering any opinions on a direction to go to in the future.

Concerning option #4, private distributors to fill and distribute special orders, would alleviate a major licensee complaint. Assuming that the Maryland Beverage Journal would apply, licensees would have a greater selection of wines, lower prices by eliminating a tier of mark up, quantity deals that might be available and probably credit terms. Special orders are very difficult to manage in the DLC warehouse because when they are received, they have no warehouse location, therefore when pulled to be delivered are difficult to find. Because of this, my reps get hammered when expected deliveries are not received on time.

The differences between DLC and private distributors are more than a few, but it's only the customer service function that is severely lacking in MoCo. At best the DLC customer service department is an order department with very little customer service. They do not have the ability to answer any questions concerning an order once it is placed. I gave up on that department years ago. Under the new system begun February, when my rep is asked by a licensee where their order is, we end up calling a warehouse manager or the Director of Operations, There is no go to person and because getting answers to licensee questions is difficult, it reflects negatively on my reps

Similar to the distributor I work for, there are many good loyal hard working people working for the DLC. My opinion and that of my seven reps, fix special orders and create a real customer service department.

Bob Mutschler

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**From:** Ferber, Justina [mailto:Justina.Ferber@montgomerycountymd.gov]  
**Sent:** Thursday, March 12, 2015 10:29 AM  
**To:** Mutschler, Bob  
**Subject:** FW: March 20th Meeting

Thank you for being willing to share your experience with the Montgomery County Liquor Control Committee. In anticipation of the worksession March 20, I wanted to share some information with you.

First, the logistics of the worksession are as follows:

**Time/Date:** 9:30am, Friday, March 20, 2015  
**Location:** Council Office Building  
3<sup>rd</sup> Floor Hearing Room  
100 Maryland Ave.  
Rockville, MD 20850  
**Parking:** There is a public parking lot adjacent to the Council Office Building that you may use.  
**Metro:** The Council Office Building is a 5-10min walk from the Rockville Red Line Station  
**Contact:** Tommy Heyboer in Councilmember Riemer's Office

5



March 26, 2015

Montgomery County Council  
Ad Hoc Committee on Liquor Control  
Attn: Hans Riemer, Committee Chair  
George Leventhal, Council President  
Marc Elrich, Public Safety Committee Chair  
100 Maryland Ave., 5<sup>th</sup> Floor  
Rockville, MD 20850

Esteemed Councilmembers Riemer, Leventhal, and Elrich:

Thank you for inviting me to submit written testimony regarding my thoughts on options for the control and distribution of alcohol within Montgomery County, Maryland. As the Chair of the Montgomery County Alcoholic Beverages Advisory Board (ABAB) and a Montgomery County resident for 14 years, I welcome the opportunity to provide my perspective on some of the proposed changes as outlined in the OLO report, "Review of Alcohol Control in Montgomery County" released in February, 2015.

In order to provide a context, the mission of ABAB (per Maryland Annotated Code, Article 2B, Section 159C, Chapter 832) is to report to the County Executive and County Council on recommendations for improvement of alcoholic beverage control and enforcement issues in the County. Members serve four-year terms without compensation and must be residents and registered voters of Montgomery County. ABAB is a five-person board, with three members from the general public; one holder of either a Class B or C beer, wine and liquor license in Montgomery County and one holder of any other class license in Montgomery County.

While I have not been able to attend all of the previous hearings, I did attend the March 20<sup>th</sup> hearing in which various concerns and complaints were expressed by retailers in Montgomery County, specifically in relation to the ordering and delivery of special order products within the County. As Chair of ABAB, I was surprised to learn about these problems. I have served on ABAB since 2008, and to my knowledge none of the issues described have been brought before the Board in the time that I have served on the Board. The issues that we have discussed and made recommendations on as a Board include the following:

- The quality of the fleet trucks used to deliver products to licensees in the County, with retailers receiving damaged products due to water getting into the trucks during rain and snow
- Opening County stores on Sundays
- One individual retailer who came to a couple meetings to discuss the mark-up process for products within the County

It is my hope that retailers as well as community members at large would see ABAB as an appropriate forum for expressing their concerns and recommendations for improving the

Department of Liquor Control (DLC). In addition, we also currently have a vacancy on the Board at this time for a holder of a Class B or C license in the County. The position was first opened in January, and no applications were received. The position was re-opened in March, with the closing date of March 23, and I have not yet heard whether any applications were received. Since this Board is required to exist by state law, I encourage license holders to become active on the Board so that their concerns can be represented and hopefully resolved in a more proactive manner before attempting to overhaul the entire Department of Liquor Control. I am in complete agreement that customer service and modernization of the DLC system is in order, and it is my belief that ABAB can help provide guidance and recommendations to the County Executive and County Council on these matters. Unfortunately, no one has reached out to us to ask for this assistance or our feedback for either the OLO report or the DLC strategic business plan.

I understand that a new software system was rolled out in February 2015 to hopefully improve some of the quality control issues with ordering and receiving products. I encourage the County Council members to give the Department of Liquor Control adequate time to see if this system is going to eliminate some of the past concerns. In addition, if this system is not appropriate for the sale and distribution of alcoholic beverages, the DLC must have the authority to run more like a business by purchasing software systems that meet their needs and by extension, the needs of retailers and consumers within the County. In this sense, I am most in support of Option 5 (Increase Efficiency within Current Structure) as outlined in the OLO report, and can state that the ABAB members will assist in as helpful a manner as possible to make the recommendations in the Long-Range Strategic Business Plan become a reality.

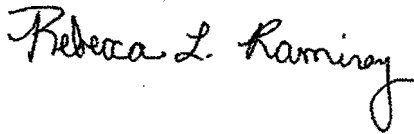
I was pleased to hear Councilmember Riemer state at the last hearing (on March 20) that there seems to be consensus to not change the manner in which distilled spirits are distributed and sold within the County. It appears that Option 4 (Private Wholesale Distribution of Special Order Beer and Wine) is the direction in which the Ad Hoc Committee is most interested in exploring, and I was specifically asked to provide my thoughts on that option. From a public health perspective, here are the questions/concerns I have with Option 4:

- What mechanisms would be put in place to define what constitutes a special order product? The DLC would need to have oversight of these product lists and the quantities being ordered, so as to preclude almost all beer and wine products from being listed as "special orders."
- How will potentially dangerous new products be prevented from being included on a product order list by distributors? In the past, the DLC has had the authority to choose not to list products (e.g., Four Loko, jello shots, etc.) that can either be potentially attractive to youth or have dangerous serving sizes or other concerns (e.g., stimulants mixed with alcohol, product labeling that makes it appear that the product isn't an alcoholic beverage, etc.)
- Will the DLC (and by extension the Board of License Commissioners) have the regulatory authority to license, enforce, and if necessary, adjudicate violations by

distributors should there be undue influence by private distributors on retailers that prevents a fair, yet competitive, market?

In summary, I encourage retailers to become more active in ABAB; I believe that Option 5 should be implemented before considering other options, and I have concerns that Option 4 will eventually result in the complete private distribution of alcoholic beverages in Montgomery County. I hope that my feedback on the suggested proposals and role of ABAB in future discussions is helpful. Please feel free to contact me should you wish to discuss any of these ideas in more detail.

Sincerely,

A handwritten signature in cursive script that reads "Rebecca L. Ramirez". The signature is written in dark ink and is positioned below the word "Sincerely,".

Rebecca L. Ramirez, MPH  
Chair, Montgomery County Alcoholic Beverages Advisory Board

Hello,

Thanks for taking the time and effort to listen to the licensees on 3/20. I was supposed to speak in lieu of the Quarry House but did not get in touch in time to be up on the panel. I own Gilly's in Rockville which is a class D on/off premise establishment. I was born, raised, and currently live in Montgomery County, we went to public school and will be sending all 3 of our children to public school as well. We are appreciative of the quality schooling/police that this county has to offer. We have 14 fantastic employees at Gilly's. In 2014 our Beer/Wine Cost of Goods Sold was well over \$500,000.00. We are small in size but I would say a very good customer of the DLC. The culture of the DLC is that we (licensees) are a pain in their ass and we just need to shut up and take what we get. I will say that the licensing department has been a pleasure - I call them when no one else is answering the phone, which is often.

The licensees on the panel brought up some good points, however I was a little disappointed with some of their arguments. Rather than get involved in small things like glassware, timing of drivers and whether or not DLC is "unamerican" there were some major issues that did not get enough attention.

1. **New Online Ordering System** - complete shambles and waste of money thus far. We are getting communication from the DLC that they are working on items, they have even provided a "hotline" phone # to call about delivery questions. The first thing I did was call the hotline - no answer - as I suspected. With the license we have, finding a suitable POS system has been a challenge. I cannot imagine what sort of system would be needed for the DLC - although I know there is one out there. This is a square peg in a round hole situation. Lets cut our losses and move on, it's been a few months of utter disaster!

2. **COD Payments** - Payment terms would be fair, even if it was 15 days. Or some sort of discount for paying COD. Budgeting is near impossible. Also with this new system, having money yanked from our bank account is not ideal. Not one of my deducted payments has matched up to what our invoice says it should be (even after doing the math with all of the shorted cases and broken bottles). I could hire a full time person just to keep track of DLC deductions in my bank account. So, not only can I not live by a budget, I am having to wait for credits which is more of my cash tied up unnecessarily.

3. **Special Orders** - my business is 95% special order. No one discussed quality control at the DLC - there is none. When they moved to the new temperature controlled warehouse - last summer we heard from several drivers that they (powers that be) did not use the air conditioning in the warehouse in order to save money!!! Our customers come to us for the newest, most limited and exclusive products available. We have to support the core brand all year long in order to be eligible to get these products. If the distributor could deliver this product in a safe, controlled and timely manner, that would be fantastic. As it is now, with the way the timing in the county works, we are about 3 weeks behind the rest of the country on limited release items (it's quite embarrassing). I would happily pay a tax or fee to the county if I was sure that my product would be delivered correctly, on time and in tact. Option #4 of the OLO sounds perfect. I speak to many breweries on a daily basis - begging them to consider coming into the county. Do you know that the way we (MOCO DLC) handle business makes us laughing stock of the industry? We are often called the third world country of the beer/wine world. Very sad.

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4. **DLC Retail Stores** - Direct competition with private stores, they are selling refrigerated product, non alcoholic product, advertising, and carrying special order items and retailing said product at basically our cost. How are we to compete and run a successful business? At least sell product at what the private stores are selling it for (win/win). I also think that DLC stores should not be able to be located within a certain mileage of private competition, especially retail stores. This would obviously be hard to track as stores come and go every day but an attempt at a non-compete option would be great. Several years ago in the early 2000's, there was a rule that the DLC retail stores were not permitted to sell anything but "stock" non-refrigerated alcohol. Why did this rule change?

5. **Liquor** - Most breweries are now diving head first into the liquor business. The DLC stores are not carrying any of these specialty/craft liquors that the consumers are looking for. Truly a missed opportunity to make some serious money. I would love to sell liquor retail at Gilly's - just the craft stuff. I would love to offer tastings of it, I would not be interested in selling liquor drinks, however I think a Class D License should have the option to sell liquor drinks in addition to beer wine. Maybe make this an addendum to the license with a new fee just as it was done with the growler law.

6. **Grocery Stores and Total Wine** - I am adamantly against these two huge entities being anywhere near this county. I live in Olney and saw what the Safeway did to the small stores in that community. I believe the wine sales at the DLC retail store in Olney also suffered a loss of business, good thing they had their liquor sales to fall back on. Our store would not have survived a "safeway" coming anywhere close to us. I understand the 1 license for big corporate business in the county and am fine with that but if every location were able to obtain a license, we would have a serious problem with maintaining small business.

In closing, the revenue from the DLC each year goes towards some good things in the county. I realize this. I would be in support of option #4 to start. It would be the best scenario, for the group of licensees who seem to really be having the most trouble with the DLC in it's current state. I am proud to say that we follow the rules given to us, I am a proud resident and business owner of MOCO. As a consumer and a business owner, I would like to be treated with a little more respect in regards to the alcohol industry. I would like to keep my money in this county and not have to shop in other counties and states for the items that should be available to us but are not (for no good reasoning!!).

Please don't hesitate to get in touch regarding this issue. I have two toddlers and another on the way so my time is a bit divided, but I will happily make this issue my priority in order to get these important changes made.

Thank you,  
 Johnna Gilchrist  
 301-661-4612 (cell)  
 Gilly's Craft Beer & Fine Wine  
 2009 Chapman Ave.  
 Rockville, MD 20852  
[Gilly's Website](#)

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**LICENSED BEVERAGE DISTRIBUTORS OF MARYLAND, INC.**

Leadership in Industry Cooperation

P.O. Box 1668

Annapolis, MD 21401

**Members**

**RELIABLE CHURCHILL LLP  
REPUBLIC NATIONAL DISTRIBUTING  
COMPANY, LLC**

**ROBERT C. DOUGLAS, Counsel**

March 19, 2015

Councilmember Hans Riemer  
Council Office Building  
100 Maryland Avenue  
Rockville, MD 20850

Councilmember Marc Elrich  
Council Office Building  
100 Maryland Avenue  
Rockville, MD 20850

Councilmember George Levanthal  
Council Office Building  
100 Maryland Avenue  
Rockville, MD 20850

Dear Councilmembers of the Ad Hoc Committee on Liquor Control,

The Licensed Beverage Distributors of Maryland have followed your conscientious review and discussion of the Montgomery County Department of Licensed Beverage Control (the "Department") by the Ad Hoc Committee (the "Committee"). As you know, we deliver more than 95% of the wine and spirits to licensees across Maryland. Our role in Maryland gives us special insight into the alcoholic beverage industry. As such, we are writing to provide information on how the wholesale industry operates thinking that information may help in your deliberations and efforts to improve the system in the County.

First, as the report of the Office of Legislative Oversight notes, Maryland has a three-tier system. The first tier are the suppliers of beverages (mainly distillers, brewers or wineries). The second tier are the wholesalers who distribute to retailers, who are the third tier, and sell to consumers. Wholesalers are licensed in Maryland to deliver requested alcoholic beverages to licensed retailers (on-premise and off-premise establishments, including bars, restaurants and package good stores). The delivered alcoholic beverages are purchased by a wholesaler from a licensed supplier, usually a winery, distillery or brewer, who form the first tier. The wholesaler collects on behalf of the state the excise tax imposed on all the alcoholic beverages by Maryland law. The excise tax is then paid to the state by the 10th of the following month.

In Montgomery County, deliveries to licensees in the County are made by the Department. Under Maryland law, the Department can purchase directly from a supplier and thereby eliminate the private wholesale tier. This enables the Department to purchase goods at the same price as a private wholesaler because Maryland law requires suppliers to charge the same price to all

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purchasers. The Department thereby purchases at a price lower than if it had purchased from a wholesaler. This enables the Department to generate higher profits.

Licensed wholesalers deliver to the Department beverages not usually carried by the Department but ordered special by a licensee. The special orders first are placed by retailers with the Department, transmitted to the wholesaler and then the special ordered beverages are delivered by the wholesaler as part of the next regular delivery to the department. These deliveries are made at least once per week. The special order is then delivered to the licensee by the Department on its regular delivery schedule to the licensee.

It is our understanding that the Committee is considering several options which would affect the existing wholesale delivery system. The options include:

Option	Est. fiscal Impact \$ Millions	Est. County Position Reductions
<b>Option 1: Full Deregulation</b> Fully deregulate alcohol control system in Montgomery County and allow private wholesale distribution and private retail sale of beer, wine and liquor	One-Time: +\$66-\$76 Ongoing Annual: (\$32-\$43)	Total: 393 Full-Time: 236 Part-time: 157
<b>Option 2: Private Wholesale of Beer/Wine/Liquor</b> Allow private wholesale distribution of beer, wine, and liquor to alcoholic beverage licensees, while maintaining County control of the off-premises retail sale of liquor	One-Time: +\$29-\$39 Ongoing Annual: (\$18-\$21)	Total: 165 Full-Time: 134 Part-Time: 31
<b>Option 3: Private Wholesale of Beer/Wine</b> Allow private wholesale distribution of beer and wine to alcoholic beverage licensees, while maintaining County control of the wholesale and off-premises retail sale of liquor	One-Time: +\$2-\$3 Ongoing Annual: (\$18-\$23)	Total: 123 Full-Time: 99 Part-Time: 24
<b>Option 4: Private Wholesale of Special Order Beer/Wine</b> Allow private wholesale distribution of special order beer and wine products, while maintaining County control of the wholesale and retail structures for all other alcohol products	One-Time: +\$0.17 Ongoing Annual: (\$4-\$6)	Total: 15 Full-Time: 11 Part-Time: 4

<u>Option 5: Increase Efficiency within Current Structure</u> Maintain the current structure of liquor control and enhance DLC's effectiveness and efficiency by adopting recommendations made as part of DLC's long-range strategic business plan.	None specified	None specified
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Here is how each of these options would function based on state-wide wholesale practices.

Options 1, 2 and 3 are consistent with existing operating procedures elsewhere in the State. Private wholesalers deliver wine, beer or spirits directly to retailers, bars or restaurants in all other jurisdiction of the State. Option 3 is the wholesale model employed in Worcester County prior to July 1, 2014 when the private wholesalers were allowed also to deliver spirits to licensees.

Option 4 does not work with existing wholesale practices. It appears that Option 4 contemplates that wholesalers would deliver special orders directly to the licensee. This would require the wholesaler to make a special trip to whomever placed a special order. In other jurisdictions, special orders are simply part of the regular order process and delivered during the regularly-scheduled stop. There are no regularly-scheduled stops by private wholesalers in Montgomery County other than to the Department because regular deliveries to licensees are made by the Department. Under Option 4, a wholesaler would have to make a special trip to the licensee making a special order. Simple economics makes this impractical and impossible. The expense of diverting a driver and truck to a distant location for the delivery of a special order, which by its nature is a small order such as a case of wine, far exceeds the profit of such a delivery. A wholesaler could not charge a special delivery fee in Montgomery County for special orders because it has to charge all Maryland licensees the same price for the product and delivery no matter the location of the licensee. (There is a minimum order requirement for regular customers, but it would not cover the expense of a special order delivery in Montgomery County.)

Having wholesalers make the special order deliveries also would not necessarily eliminate a wait time. The special order is delivered to the Department by the licensee and then within a week the wholesaler delivers the special order to the Department as part of its regularly-scheduled delivery. In any event, there is a waiting period for receipt of a special order. In the current system, the wholesaler has no involvement with the delivery to the licensee once the product is delivered to the Department. The special order is delivered to the licensee by the department. If there is a lag time in the final step of the process, it could be solved by the licensee picking up the product from the Department or the creation of a special order delivery vehicle at the Department which would make deliveries the day the product arrives at the Department. In either case, the licensee would not have to wait for the delivery once the product is on the Department shelf.

The bottom line is that Option 4 will not work for a simple reason: wholesalers are not required to make a money-losing delivery simply because an order is placed. Wholesalers most likely would not deliver a special order because they would to lose money. In short, Option 4 is not the solution to the special order issue in the County.



As a final discussion, we would like to provide insight on the suggested revenue plans. Any increase in the cost of a beverage product will reduce sales in the County because it is so easy to go elsewhere and purchase the same product for less. Montgomery County is bordered by several jurisdictions with lower prices and any increase in prices will further erode sales in the County. As such, an increase in sales or excise taxes, imposing a special fee based on volume or charging wholesalers a fee, is counter-productive. The report by the Office of Legislative Oversight begins with a discussion of cross-border sales and estimates that Montgomery County loses between \$46 million and \$186 million in sales because residents shop for lower prices out of the County. Increasing the cost of alcoholic beverages will not solve this problem, rather it will accelerate losses. In other words, Montgomery County cannot increase its profits by making its products more expensive in a competitive marketplace.

We appreciate the thoroughness and thoughtfulness of the Committee's work. If there is any other information we may provide to help the Committee in its deliberations, please let us know.

Sincerely,

James M. Smith  
Kevin Dunn  
Reliable-Churchill LLLP

Joel Polichene  
Thomas White  
Republic National Distributing Company

Cc: Robert C. Douglas, Esquire

# The Country Vintner

A member of The Winebow Group



May 4, 2015

Councilmember Hans Riemer  
Council Office Building  
100 Maryland Avenue  
Rockville, MD 20850

Councilmember George Levanthal  
Council Office Building  
100 Maryland Avenue  
Rockville, MD 20850

Councilmember Marc Elrich  
Council Office Building  
100 Maryland Avenue  
Rockville, Maryland 20850

Dear Councilmembers of the Ad Hoc Committee on Liquor Control:

I am writing to you on behalf of The Country Vintner, LLC (TCV) in response to a request by Councilman Hans Riemer's office for input regarding the feasibility of various options under consideration to change Montgomery County's alcohol control structure as discussed in the Office of Legislative Oversight Report 2015-6 (OLO Report) dated February 10, 2015. For your information, TCV currently sells stock and special order items to the Montgomery County Department of Liquor Control (DLC) and through that relationship has made fine wine and craft spirit products available to Montgomery County retail licensees and consumers for more than 10 years.

As summarized in the OLO Report, Montgomery County, through the County's DLC, is the only "control" jurisdiction in Maryland. As a control jurisdiction, DLC is the exclusive wholesaler of alcoholic beverages in the county buying beer, wine and liquor from producers (and sometimes other wholesalers and importers) and reselling to retail outlets in the County. Montgomery County also has exclusive authority over the retail sale of liquor which it sells at 25 County-owned and operated stores. All other Maryland counties are "license" jurisdictions where private sector businesses receive licenses to sell alcoholic beverages at wholesale and retail. Thus, in contrast to every other county in Maryland, deliveries to retail licensees in Montgomery County are made by the DLC, and not by licensed wholesalers.

DLC inventory is categorized as stock or special order. Stock items are carried routinely and ordered by DLC on a recurring basis to fulfill projected retail demand and are typically delivered on a licensee's next scheduled delivery day. Special order items are not regularly

carried as inventory in DLC's warehouse, but are purchased by DLC in response to a specific order from a licensee, retail store, or customer at a retail store. The time it takes for DLC to receive and deliver special order items is highly variable.

We understand that the Committee is in the process of reviewing and several options for structural changes to Montgomery County's existing wholesale delivery system, as well as the budgetary/fiscal impact of the proposed changes. To the extent that change is deemed warranted by the Committee, we advocate Option 4 below as the best of the proposed options.

Option	Est. fiscal Impact \$ Millions	Est. County Position Reductions
<b><u>Option 1 Full Deregulation</u></b> Fully deregulate alcohol control system in Montgomery County and allow private wholesale distribution and private retail sale of beer, wine and liquor	One-Time +\$66-\$76 Ongoing Annual (\$32-\$43)	<b>Total 393</b> Full-time 236 Part-time 157
<b><u>Option 2 Private Wholesale of Beer/Wine/Liquor</u></b> Allow private wholesale distribution of beer, wine, and liquor to alcoholic beverage licensees, while maintaining County control of the off-premises retail sale of liquor	One-Time +\$29-\$39 Ongoing Annual (\$18-\$21)	<b>Total 165</b> Full-Time 134 Part-Time 31
<b><u>Option 3 Private Wholesale of Beer/Wine</u></b> Allow private wholesale distribution of beer and wine to alcoholic beverage licensees, while maintaining County control of the wholesale and off-premises retail sale of liquor	One Time +\$2-\$3 Ongoing Annual (\$18-\$23)	<b>Total 123</b> Full-Time 99 Part-Time 24
<b><u>Option 4 Private Wholesale of Special Order Beer/Wine</u></b> Allow private wholesale distribution of special order beer and wine products, while maintaining County control of the wholesale and retail structures for all other alcohol products	One Time +\$0.17 Ongoing Annual (\$4-\$6)	<b>Total 15</b> Full Time 11 Part Time 4
<b><u>Option 5 Increase Efficiency within Current Structure</u></b> Maintain the current structure of liquor control and enhance DLC's effectiveness and efficiency by adopting recommendations made as part of DLC's long-range strategic business plan	None specified	None specified

As summarized above, Option 4 would allow the private wholesale distribution of special order beer and wine products, while maintaining County control of the wholesale and retail structures for all other alcohol products. Under Option 4, wholesalers such as TCV would deliver special orders directly to the licensee. Contrary to assertions made by the Licensed Beverage Distributors of Maryland, Inc., Option 4 is economically viable and there would be no

extraordinary financial burden associated with making special order deliveries directly to retailers in Montgomery County, just as deliveries are made direct to retailers in the ordinary course in every other locality in the state. Although DLC special order sales are relatively small by quantity sold, they account for approximately one-fifth of both wholesale and retail sales revenue (\$28.2 million in wholesale sales revenue for FY14; \$21.9 million in retail sales revenue in FY14) (OLO Report p. 31). Of 29,000 different items available for purchase on DLC's product list, approximately 85% (24,895) are special order items. (OLO Report p. 56). If adopted, Option 4 would be beneficial to Montgomery County because it would remove a labor intensive and burdensome line of distribution from the County and would give TCV direct access to retail licensees, which in turn would provide greater access to a variety of products and increased ability to compete within the regional market.<sup>1</sup> The citizens of Montgomery County will also benefit from increased access to a greater variety of high quality products, and from the increase in tax revenue generated within the county associated with the sale of these products.

Not only does TCV favor Option 4, but the licensee survey conducted by OLO indicated that 87% of respondents favor allowing licensees to purchase special order beer and wine from private wholesalers. (OLO Report p. 53). This option received the most support of all of the options considered.<sup>2</sup> (OLO Report p. 81). The ability of wholesalers to make the special order deliveries would make products available to retail licensees and ultimate consumers much more quickly and efficiently since the licensee would not have to wait for the DLC to deliver the special order as part of its regularly-scheduled delivery. Although it had been hoped that DLC's new warehouse management system implemented on February 1, 2015 would improve communications and the ordering process, particularly for special order products, there is continuing frustration with the new system and an increase in delays associated with getting special order products to retail licensees and the ultimate consumers. Implementing Option 4 would provide DLC with an increased opportunity to focus on and implement other strategies to help ensure the long-term success of its remaining operations.

In addition to the above, Option 4 is expected to have the least financial impact on the County of any of the other options proposing structural change to Montgomery County's alcohol distribution structure. It is also expected to have a much smaller impact on county jobs compared to other options affecting structure (estimated total of 15 jobs lost as compared to the Options 1, 2 or 3 which range from 123 to 393 jobs lost).<sup>3</sup> Although there would be some relatively minimal revenue loss associated with the implementation of Option 4, we believe that these losses would be offset by improved availability, selection, and pricing for alcohol products

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<sup>1</sup> It is believed that Montgomery County retail licensees lose sales revenue to stores and restaurants in neighboring jurisdictions (particularly Washington, D.C. and Virginia) due to better availability, selection and pricing of alcoholic beverages in those locations. (OLO Report p. 86).

<sup>2</sup> OLO Report indicated that most interviewees expressed dissatisfaction with DLC's process for ordering special order products reporting that it could take weeks to months for DLC to receive and deliver items. (OLO Report p. 80). Several retail licensees reported a desire to stock items that are available only through special order, but indicated they stock fewer or no special order products because of the difficulties and time involved in getting the products (OLO Report p. 80).

<sup>3</sup> It is also possible that DLC could reduce these positions over time through natural attrition. (OLO Report p. 99).

for retailers and consumers; enhanced profitability and effectiveness of current restaurants and retail establishments in the County; enhanced desirability of Montgomery County as a location for new restaurant and retail establishments; and a more profitable and vigorous food service and alcohol retail industry. (OLO Report p. 86). For the record, we would not be in favor of increasing the cost of beverage products through taxation or otherwise since this would likely erode sales in Montgomery County where cross-border sales (mentioned above) have been identified as a serious concern.

Thank you for your dedicated review and consideration of the OLO Report and our comments set forth above. Please do not hesitate to contact me should you have any questions or need any additional information.

Sincerely,

A handwritten signature in dark ink, appearing to read 'Matthew Tucker', with a large, sweeping flourish extending to the right.

Matthew Tucker  
Vice President of Business Development  
North Mid-Atlantic



A Sheehan Family Company

May 28, 2015

Councilmember Hans Riemer  
Council Office Building  
100 Maryland Avenue  
Rockville, MD 20850

Councilmember George Levanthal  
Council Office Building  
100 Maryland Avenue  
Rockville, MD 20850

Councilmember Marc Elrich  
Council Office Building  
100 Maryland Avenue  
Rockville, Maryland 20850

Dear Councilmembers of the Ad Hoc Committee on Liquor Control:

I am writing to you on behalf of Legends Limited Beer Distributing to provide feedback relating to various options to change Montgomery County's alcohol control structure set forth in the Office of Legislative Oversight Report 2015-6 ("OLO Report) dated February 10, 2015. For your information, Legends currently sells only special order items to the Montgomery County Department of Liquor Control (DLC).

In 1994, Legends Limited stated when Pat and Sherri Casey could not find a distributor in the Maryland that would carry their imported European beer brands. So Pat and Sherri decided to start a beer distributing business themselves. Legends' first warehouse was located at the old National Brewery building in Brewers Hill, Baltimore. We began servicing the Washington D.C. market in 2006. In 2009 we were acquired by the Sheehan Family Companies. We are now the 7th largest Maryland distributor, based on employees. Today, Legends portfolio now represents over 100 brewers not only from Europe but from other counties around the world such as Lebanon, Russia, Kenya, Brazil, El Salvador and India. We have also embraced the rise in craft brewers right here in the our own region and across the country representing brands such as

Stillwater and Union Craft Brewing from Baltimore, Blue Mountain from Virginia, DC Brau, from Washington, DC. We also distribute Allagash from Maine, to Lagunitas from California and many in between. The rise in craft beer has allowed Legends to grow and create new good paying jobs with full benefits within Maryland.

As summarized in the OLO Report, Montgomery County, through the County's DLC, is the only "control" jurisdiction in Maryland. As a control jurisdiction, DLC is the exclusive wholesaler of alcoholic beverages in the county buying beer, wine and liquor from producers (and sometimes other wholesalers and retailers) and reselling to retail outlets in the County. Montgomery County also has exclusive authority over the retail sale of liquor, which it sells at 25 County-owned and -operated stores. All other Maryland counties are "license" jurisdictions where private sector businesses receive licenses to sell alcoholic beverages at wholesale and retail. Thus, in contrast to every other county in Maryland, deliveries to retail licensees in Montgomery County are made by the DLC, and not by licensed wholesalers.

DLC inventory is categorized as stock or special order. Stock items are carried routinely and ordered by DLC on a recurring basis to fulfill projected retail demand and are typically delivered on a licensee's next scheduled delivery day. Special order items are not regularly carried as inventory in DLC's warehouse, but are purchased by DLC in response to a specific order from a licensee, retail store, or customer at a retail store. The time it takes for DLC to receive and deliver special order items is highly variable. **Every one of Legends products is considered a special order.**

Distributing and storing beer properly is different than distributing wine or spirits. Wine and spirits have a much longer shelf life, does not require cold storage, does not incur a large seasonal or special release packages and does not have the high rate of rotation of tap lines in bars or package placements at retail. This presents special issues for the Montgomery County Department of Liquor Control and Legends. Legends has had difficulty in the past with our special order stock going out of code in the DLC's warehouse, abiding to proper credit terms and getting delivery to the retailer in a timely manner.

We understand that the Committee is in the process of reviewing and several options for structural changes in Montgomery County's existing wholesale delivery system, as well as the budgetary/fiscal impact of the proposed changes. To the extent that change is deemed warranted by the Committee, we advocate for Option 5 and Option 4 as the best of the proposed options.

Option 5 "Increase Efficiency within Current Structure" should be undertaken as soon as possible regardless of the other four options. There are many ways to increase the efficiencies of the warehouse and deliveries by embracing and using commonly used systems that are currently used by private distributors such as Legends. Increase efficiency means increased profits and in the end an increased revenue stream for Montgomery County and its residents.

Option 4 "Private Wholesale of Special Order Beer/Wine" would allow private wholesale distribution of special order beer and wine products, while maintaining County control of the wholesale and retail structures for all other alcohol products. With the difference noted above between beer and spirits and wine the county should seriously consider implementing this options as well. Under Option 4, wholesalers such as Legends would deliver special orders directly to the licensee. Option 4 could be economically viable. It may be worth the investment by Legends to invest in an additional truck and personnel to make special order deliveries directly to retailers in

Montgomery County, just as deliveries are made direct to retailers in the ordinary course in every other locality in the state. This option would allow better control of our products and further guarantee a timely delivery for our customer in the county.

Thank you for your dedicated review and consideration of the OLO Report and our comments set forth above. Please do not hesitate to contact me should you have any questions or need any additional information.

Sincerely,

Erin Tyler  
General Manager  
Legends  
A Sheehan Family Company