Workgroup on Montgomery County Department of Liquor Control
Minutes
Thursday, July 14, 2016
1:00 pm – 3:00 pm
1401 Rockville Pike, Lobby Level, Rockville, MD 20850

Participants

Workgroup Members Present:

Brian Vasile, Managing Partner, Brickside Food and Drink
Pinky Rodgers, Owner, Pinky & Pepe's Grape Escape
Nick Manis, Deputy Director, National Beer Wholesalers Association
Joseph A. Giardina, Division Manager, Breakthru Beverage
Gino Renne, President, Municipal and County Government Employees Organization (MCGEO)
Ken Silverman for Hans Riemer, Montgomery County Councilmember
Jennifer Hughes, Director, Montgomery County Office of Management and Budget (OMB)
Fariba Kassiri, Interim Director, Montgomery County Department of Liquor Control
Kevin Atticks, Founder, Grow and Fortify; Executive Director, Maryland Wineries Association/Brewers Association of Maryland/Maryland Distillers Guild
Delegate Charles Barkley, Montgomery County Delegation
Alex Espinosa, Director, (appointee) Montgomery County Department of Finance

Guest Presenters:

David Ozgo, Senior Vice President, Economic and Strategic Analysis, Distilled Spirits Council of the United States (DISCUS)
David Wojnar, Vice President, Control States, Distilled Spirits Council of the United States Government Relations (DISCUS)
Dwayne A. Kratt, Senior Director, State Government Relation, Diageo (manufacturer)
Neal Insley, Former Chair, Virginia Alcohol Beverage Control and General Counsel to the National Alcohol Beverage Control Association (NABCA)

Minutes

The meeting was led by Bonnie Kirkland, Assistant Chief Administrative Officer for the Montgomery County Executive's Office, and began at 1:10 pm. Following the workgroup member's introductions, Ms. Kirkland explained that the workgroup will not be rehashing what occurred with the previous ad-hoc committee regarding DLC operations. She further stated that the workgroup is tasked with looking at options for different organizational models. Ms. Kirkland noted that what was made clear from the previous ad hoc committee was that privatization brings an increase in alcohol availability and with that brings more issues and costs. Ms. Kirkland explained that with that understood, the task force will not be revisiting that as a topic in order to allow for time to focus on feasible models. Ms. Kirkland stated that if there are any other presenters that attendees believe the taskforce should be hearing from, to please let her know and she will try to fit into them the schedule.

Presenter, David Wojnar, Vice President, Control States, Government Relations, DISCUS:

Mr. Wojnar explained that the association offers strategies to maximize revenue growth. Sunday sales are an example of that. Sunday sales represent a way that sales have been maximized in control states without additional costs.

Presenter, David Ozgo, Senior Vice President, Economic and Strategic Analysis Distilled Spirits Council of the United States (DISCUS):

Mr. Ozgo presented sales data (per capita sales volumes, not to be confused with consumption rates) in Montgomery County compared to Maryland as a whole, the nation and Washington DC. This data is included in a slide presentation available on the Workgroup link. According to his data, Montgomery County's per capita sales of spirits is 42% less than the state average; per capita beer sales are also well below the comparison group; and per capita wine sales are about the same as the comparison jurisdictions.

He noted that as household income rises, typically so does wine consumption. He suggested that per capita wine consumption should be higher given the high income levels in Montgomery County.

Mr. Ozgo also suggested that the County is missing out on an estimated $141 million dollars in sales. He says that the main consumer driver is convenience. In almost every control state, the experiments with Sunday sales showed increases in consumption rates just by having stores open. The number of stores stayed the same.

Nationwide, he noted, off premise sales (package stores) drive sales for beer, wine and spirits, accounting for 78% total volume. Even in tourist destinations like Nevada, off premise sales account for nearly 60% of volume. He suggested that to realize sales potential, the problems encountered at off premise stores must be evaluated.

Regarding outlet density analysis, Mr. Ozgo noted that outlet density is regularly measured per 10,000 adults. He says that nationally, there is an outlet density rate of 3.34; in Maryland (excluding Montgomery County) the rate is 3.02; Montgomery County has a rate of 0.34. Washington DC has a rate of 4.52. Montgomery County is even well below the control state average of 1.84. There is no other jurisdiction that has so few spirits outlets.

In his view, consumers crave convenience, and adding outlets is a way of capturing these sales.

In summary, Mr. Ozgo indicates that the Montgomery County per capita sales are well below the expected levels of 24-41%. High income means that residents are likely purchasing wine elsewhere. Consumers crave convenience and would like to purchase all three alcohol types at one location. There is a big opportunity for revenue by adding more outlets.

General Discussion:

In response to a question posed by Jennifer Hughes, Mr. Ozgo stated that income analysis for beer and spirits are more along the lines of average for Montgomery County but that, that analysis could be provided as well.

Gino Renne asked if the Distilled Spirits Council had worked with Pennsylvania (a control state) since they incurred cross border sales losses from big box stores opening along border states such as West Virginia (also a control state). Mr. Renne also asked if they have they helped to redesign Pennsylvania's outlet network. Mr. Wojnar answered that the DISCUS did provide input to several administrations over time, and they had also found that Pennsylvania was dramatically low in spirits outlets.

In response to a question posed by Brian Vasile on how unique Montgomery County is, Mr. Wojnar replied that Montgomery County is not really unique. He explained that all 50 states have different local alcohol components and this is nothing new. Varied alcohol laws are a common theme nationally.

Mr. Ozgo stated that through other states experimentation, Montgomery County has s an opportunity to take the best of what's happened in other states and create a model that best fits this County.

Presenter, Dwayne Kratt, Senior Director, State Government Relation, Diageo

Maryland has varied its distribution models in the past, such as Worcester County which has allowed for private wholesalers to provide alcohol.

His concept is that if that you have private wholesalers servicing on premise establishments (restaurants/bars), they may be able to it better. Private wholesalers have large warehouses and have increased product availability. However, if the County were to do that, it is recognized that revenue will go down. There is an opportunity to make that up with more off premise stores.

There is a model that allows for the County to create criteria and have off premise package stores apply as agents to sell spirits. This would not increase the number of new outlets, but rather add spirits to some already established beer and wine outlets. States that do this include Maine, Oregon, Idaho and Ohio.

He suggested that spirits could still be delivered to these stores by DLC and the current DLC stores would be kept. Pennsylvania decided that they needed to improve their stores. People here in Montgomery County don't complain about Montgomery County stores, they are nice, clean and well stocked. There just needs to be more of them. Generally, finances just don't allow for an investment in more stores. This agent model could work well.

General Discussion:

In response to Delegate Barkley's questions as to what impact agent stores would have on current DLC retail stores, Mr. Kratt stated that it would depend on where the stores are located and that a mandatory distance requirement could be set between stores. Some control states have challenges with pricing. However, prices are very competitive here in Montgomery County.

Mr. Wojnar stated that in the State of Oregon, data was provided as to where stores are needed and that these are available resources. There are a lot of people who would say you would just be diluting sales. Starbucks is a good model of where people have begun to drink more coffee because of availability. These new outlets will drive new sales. He suggested the goal be to sell more and recapture alcohol sales within the county. As it stands, Montgomery County's per capita sales are very low.

Gino Renne stated that there were compromises made on purpose in terms of convenience between the County retail stores and small mom and pop retailers. For instance, the County retail stores do not make cold beer available, don't sell mixers in an effort to not be in direct competition with the small, privately owned beer and wine stores. There are a lot of historical compromises that DLC made to small businesses and that they need to be respected.

Jennifer Hughes stated that there was a study commissioned by DLC that reported that twelve stores could be added before saturating the County. Ms. Hughes further stated that the Office of Management and Budget (OMB) realizes that within a year or two liquor stores are profitable and they give money back to the DLC's general fund transfer. Additionally, OMB has a systematic plan to open more stores, but that plan has been put on hold until current issues are resolved. Ms. Hughes expressed that she has concerns that economic analysis could bring big expectations that will not hold up as there are other considerations that may not allow numbers to come through. The numbers presented may be optimistic.

Mr. Ozgo stated that if Montgomery County were to double the number of liquor outlets the County would still only be parallel to Virginia. Additionally, the additional outlets don't have to come all at once. In Colorado, they implemented a plan to increase markets over 20 years. Montgomery County needs to set a target, it does not have to be done overnight. Phase it in. There is a need for more stores without over saturating.

Bonnie Kirkland stated that one store recently opened (Kentland's) and two more are in the works, set to open before the end of this calendar year.

Dwayne Kratt explained that agent stores may be a good model because you can add sales without adding any upfront cost. Mr. Kratt further explained that in some areas agents had considered it a birthright to sell spirits but that the County can set limitations upfront to avoid that.

Gino Renne stated that the County has in fact experimented with contracting stores in the past (Flower Ave.) and it did not work and was not repeated on purpose.

Mr. Kratt noted that beer wholesales have a franchise law, however, spirits and wine do not. The agent store concept has DLC retaining wholesale operations. Generally, sprits wholesale at a 25% profit margin, DLC will still get that. The County does not necessarily have to give up retail. A percent of the spirits sales from agent stores can be commissioned. For example, if we sell a product for $19.99, we can sell it to an agent $2 cheaper, so there is a gain for the owner.

In response to a question posed by Delegate Barkley on how the Maryland alcohol tax increase, from 6% to 9%, effected alcohol sales Mr. Wojnar stated that in Delaware, there was a complete inverse, sales fell and were made up.

Bonnie Kirkland stated that the workgroup will be looking closely at the effects of privatization including the effects on Washington State, where alcohol prices went up significantly and resulted in increased cross-border sales.

<u>Neal Insley, former chair of Virginia Alcohol Beverage Control and General Counsel for the National Alcohol Beverage Control Association (NABCA)</u>:

The National Alcohol Beverage Control Association (NABCA), is Montgomery County's national association. The association is not an advocacy group; NABCA compiles data and makes it available which can help control states and jurisdictions make decisions.

Mr. Insley stated that in the past he was appointed as Chairman of Virginia Beverage Control by Governor McDonnell. The Governor was facing transportation funding difficulties and part of the plan was looking at privatizing Virginia to generate a cash flow to be able put towards transportation. As time went on there were more and more caveats presented to get this up front money. They didn't want a price increase for alcohol, they didn't want the annual revenue stream from liquor control to stop. Additionally, the Governor's numbers were problematic in meeting these goals. There were conflicting numbers. An independent firm (PFM) was charged to look at the numbers and it became apparent that all the criteria could not be reached under privatization. Virginia looked at the privatizing agency stores concept as well.

Working on a national level, the 21st amendment allows each jurisdiction to decide what works best for them. A good discussion, such as the one this workgroup is involved in, is key to that.

Diageo and the Distilled Spirits Council, did a good job presenting numbers, but there is a need to make these numbers specific to your jurisdiction.

Takeaways:

1. Fully vet the numbers, your jurisdiction and your constituents
2. Identify variables
3. Be conservative with numbers, remember that it is impossible, or near impossible, to put genie back in bottle
4. Engage all stakeholders (police, public safety and public health should have prominent roles)
5. Remember that on average, 40% of the population do not consume alcohol. These are still your constituents.

Budget neutrality was the goal in Virginia, and this was not a possible with privatization. It was difficult to keep the agency from imploding from the weight of the discussion.

The final determination in Virginia was that they decided they like the system they have and they wanted to make it better. The authority bill came from that. Passed in 2015, the bill changed the agency to a standalone authority, allowing them to act like a business.

It created a publicly traded corporation instead of a board, an agency head, and five appointed board members with five year terms. Before all appointees served at the pleasure of the governor, who had one term, so every four years there was a change over. A consistency in operations was needed. This also created a full time CEO, who answers to the Board and can only be terminated by cause, with no term limits. This provides consistency in operations. There was a delayed enactment to 2018.

The "rip the band aid off" approach is not the way to go. Consultants are in place to reach the 2018 goal of transitioning into an authority. This also allows the department to be taken out of procurement processes, but the authority must put grievance procedures in place for employees. Budgeting is done to be able to reinvest in warehousing, to be able to grow. The Governor still has oversight, and they are audited annually by the state.

This was a fourteen-page bill. This is a potential option for Montgomery County. There is a hodgepodge with how control states operate, Oregon has little control versus Virginia who controls all the way though, having their own retail stores. Many have a hybrid of government and agency stores. Often control states have provisions in location.

General Discussion:

Jennifer Hughes asked for a copy of the Virginia bill. Bonnie Kirkland noted that she will follow up with the bill and various related reports. They will be posted on the website (link).

In response to Kevin Atticks, who asked if NABCA had an outline of the different models for control states showing how they are currently set up, Mr. Insley stated a chart is available and that he will send it to Ms. Kirkland to share.

Bob Muncher, Sales Manager for Republic National Distributing Company, noted that Virginia stores sell sprits, some Virginia wines and a limited selection of mixers and other items.

Brian Vasile stated that businesses in VA need to pick up their spirits from the Virginia ABC stores. Virginia does not provide product delivery.

Mr. Insley stated that was true, that Virginia had looked at the feasibility of delivery and had to upcharge. On premise accounts (restaurants/bars) would rather have prices be lower and pick up product themselves.

In response to a question posed by Nick Manis, Mr. Insley stated that in Virginia there are private wholesalers and the state does not wholesale wine and beer.

Bonnie Kirkland asked the workgroup if there were any other groups that should be considered for a presentation.

Brian Vasile, said he would like to hear more unbiased information about financial impacts because the issue is about revenue. Ms. Kirkland stated that one of Mr. Leggett's major concerns is to find a way to generate this revenue that the county depends on and that he has made that public.

Ken Silverman stated that adding taxes or fees to the cost of alcohol was something that was looked at but had proved to be a stumbling block for legislation. Mr. Silverman noted that it would be helpful to have the economic impact evaluated.

Delegate Barkley stated that presentations from retailers would be helpful. He noted that he knows of one who would be willing to give a presentation. Delegate Barkley further stated that if the current system is kept it needs to be determined that it can be improved to work for them. The DLC is getting better but is still not where it needs to be.

Pinky Rodgers then stated that she keeps hearing people say it's getting better but that it has not. Ms. Rodgers held up a stack of pictures and invoices and said that of the last nine deliveries she received, eight have had issues including short on trucks or breakage.

Delegate Barkley asked Ms. Rodgers, remarking that her business consists of a lot of high end special order wines, if she thinks her experience is different than it would be for other business within the County. Ms. Rodgers stated that she has multiple pictures of trucks with ruined product due to rain getting into the trucks and ruining the boxes. Ms. Rodgers stated that she should be able to place an order and receive a delivery and have it in a state that it can be sold and have all the product ordered delivered at one time.

Ms. Fariba Kassiri explained that Ms. Rodgers seems to be an outlier and that her claims are not what the statistics show. The Oracle system tracks product and delivery, in fact it is a County Stat measure and she would like to have those numbers brought before the workgroup. Currently delivery accuracy for special order wine has risen to 85%.

Bonnie Kirkland noted that a huge part of the ad-hoc committee time was devoted to licensees testifying about these types of issues and that in the meantime, DLC has been charged with continuing improvements.

Gino Renne stated that he has been struggling with issues with the DLC since 1995. In response to Ms. Rodgers, Mr. Renne further stated that it is not lost on the union that you are clients, you need to generate income and feed your families but let's not cast stones. Some licensees have treated DLC staff horribly, remember that no operation is perfect. Striving for a mutual goal is the best way to serve clients, despite the loud argument by a small group of people, including Peter Franchot, who has no business in this debate.

Mr. Renne went on to explain that the Department of Liquor Control is a public asset and that taxpayers own this asset. It is designed to generate revenue and, if privatized, the burden will go to the taxpayers. The County is falling short with critical services it can't pay for and the burden will be on citizens of the County. It has already been identified that there are contracted night workers that throw things on the truck. This is an operations issue that has been identified. The delivery staff does not want to show up with broken bottles; it's embarrassing to them, and it impacts their professionalism.

Kevin Atticks asked for a list of concerns, and related reports, that were raised at ad hoc committee, to be able to read for background since it is not going to be rehashed within the workgroup. Additionally, he asked for the operating budget for DLC, remarking that it would be helpful if the County is considering engaging in a private business model as private wholesales seem to be able to identify and fix issues. It will help in expanding recommendations.

Bob Muncher noted that DLC's retail and wholesale revenue is broken out. Bonnie Kirkland confirmed this and stated that it would be provided.

At this point Ms. Kirkland opened up the floor to questions from the audience.

Questions from the Audience:

Ginanne Italiano, President and CEO of the Bethesda Chamber of Commerce, asked what the time frame of the work group was.

Ms. Kirkland stated that she hopes the workgroup would conclude in September, but that if more analysis is needed it will be extended for another month. The workgroup will have to be given time to pull the discussion together and present it to the County Executive before the legislative session.

A member of the audience, Melvin Thompson of the Restaurant Association, asked if there was any thought given to surveying licensees since the DLC action plan has begun to be implemented. Ken Silverman responded that Councilmember Riemer has been in talks with OLO to do this.

Nick Manis pointed out that the next meeting on August 10th may be a difficult day for members because it is the same day as the National Conference of State Legislators.

Ms. Kirkland replied that the meeting could possibly be held at the Executive Office Building to accommodate for call ins.

The workgroup concluded at 2:50 pm.

Future Meetings:

August 10, 2016, 10:00 am -12:00 pm, Executive Office Building, 101 Monroe Street, 9th Floor, Rockville, MD 20850

CONFERENCE CALL NUMBER: 641-715-0700; access code: 206260

September 15, 2016, 10:00 am -12:00 pm, TBD