M E M O R A N D U M

September 23, 1991

TO: Andrew Mansinne, Jr., Director
Office of Legislative Oversight

VIA: Joyce R. Stern *Joyce R. Stern*
County Attorney

FROM: James L. Parsons, Jr. *James L. Parsons, Jr.*
Assistant County Attorney

RE: Requests for Opinions by the Office of Legislative Oversight Regarding the Feasibility of Contracting Out or Privatizing Elements of the Department of Liquor Control Operations

The following opinion is in response to Ms. Pedersen's memoranda dated July 25, 1991 and August 2, 1991, requesting opinions from the County Attorney concerning the feasibility of contracting out or privatizing elements of the Montgomery County Department of Liquor Control ("DLC") operations.

Specifically, Ms. Pedersen has requested advice on the following subjects: (a) whether any protections are afforded Montgomery County in Article 2B, Alcoholic Beverages, of the Annotated Code of Maryland[1] if the judgment in U.S. v. Maryland State Licensed Beverage Association, Inc. were to be vacated; (b) what legislative changes, if any, would be needed to establish DLC as an "authority or quasi-governmental unit of County government;" and (c) whether Article 2B of the Annotated Code of Maryland and/or the County Code would need to be revised to allow DLC to contract out any portion of its operations. The following analysis will address each of these questions in turn.

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[1]Md. Ann. Code art. 2B (1957, 1990 Repl. Vol.). All references to Article 2B will be by section number unless otherwise indicated.

1. U.S. v. Maryland State Licensed Beverages Association, Inc.

In the late 1950's, the Antitrust Division of the United States Department of Justice filed an action in Federal court seeking injunctive relief against manufacturers, wholesalers, retailer associations and wholesaler associations in the alcoholic beverage industry in Maryland for violations of the Sherman Antitrust Act. U.S. v. Maryland State Licensed Beverages Association, Inc., 168 F. Supp. 431 (D. Md. 1958). The evidence in that case showed that between 1947 and 1955, certain retailers, wholesalers and their respective associations conspired to require manufacturers to refrain from selling directly or through a wholesaler to DLC at prices less than the wholesalers' price to retailers. Part of the conspiracy involved the boycotting by retailers of manufacturers selling directly to Montgomery County. Id. As relief, the United States District Court for the District of Maryland ordered that the named defendants be required to sell to Montgomery County certain brands of liquor at the same price offered to other Maryland wholesalers. Id. at 442.

Your office has asked what protections are afforded Montgomery County in Article 2B, Alcoholic Beverages, of the Annotated Code of Maryland if this judgment were to be vacated. Section 108 prohibits price discrimination by liquor suppliers "between one wholesaler and another wholesaler or between one retailer and another retailer purchasing alcoholic beverages bearing the same brand and trade name and of like age and quality." The purpose behind Section 108 is "to eliminate the undue stimulation of the sale of alcoholic beverages and the practice of manufacturers and wholesalers in granting secret discounts, rebates, allowances, free goods or other inducement to selected licensees which contribute to a disorderly distribution of alcoholic beverages...."

Section 109 authorizes the Comptroller of the State of Maryland to require the filing by manufacturers, wholesalers and non-resident dealers of schedules of prices at which their wines and liquors are sold, and further to require the filing of any proposed price change. This section was designed "to eliminate price wars, which unduly stimulate the sale and consumption of wines and liquors and disrupt the orderly sale and distribution thereof...." Finally, Section 163, which specifies the powers of DLC, authorizes DLC to purchase alcoholic beverages from any licensed wholesaler, manufacturer, non-resident producer, or dealer.

Although Article 2B allows DLC to purchase liquor from distillers and prevents distillers from engaging in price discrimination against DLC, there is no requirement in the state law that requires distillers to sell to Montgomery County. In fact, Sections 108 and 109 have specific language providing that the state law does not require the distillers to sell to any licensees.

Sections 184 and 185 authorize and direct the Comptroller of the State of Maryland to publish rules and regulations to enable him to effectively discharge his duties under Article 2B. Under Regulation 03.02.01.12 published by the Comptroller, a supplier of liquor and/or wine may not select more than one wholesale licensee to distribute its product. In other words, dual distributors are prohibited in Maryland. However, the regulation does not apply to county dispensaries operating as wholesalers.

Accordingly, if the subject decree is vacated, the named distillers would be free to sell only to their exclusive distributors. Therefore, the decree entered in the Maryland State License Beverage Association case provides the sole basis for the requirement that the named distillers in the decree sell to Montgomery County at the same price offered to other Maryland wholesalers.

2. Establishing DLC as an Authority or Quasi-governmental Unit of County Government.

An authority is a statutorily created public corporation, which has attributes of both government and private enterprise. The traditional characteristics of a public corporation or authority have been described as follows:

- Each public corporation is established by a specifically written statute or charter; because each is very individual, there is no typical model.

- The public corporation is an independent body with a separate legal identity.

- Its management is in the hands of a governing board the members of which are appointed by the government rather than by individual citizens or interest groups.

- The basis of public corporation funding is from the revenues they earn rather than from appropriations authorized by a legislative body.

- In its daily operations, it is like other private legal corporate persons: it is fully liable in law and does not possess any of the legal privileges and immunities of government.

- The public corporation is dual in nature: in terms of management, it resembles private sector businesses; but because it fulfills public duties on behalf of the government, it is subject to control by the government.[2]

In addition, enabling statutes for authorities typically contain finance-related requirements such as: "(1) submission of the authority's operating budget to the executive or the legislature; (2) disposition of its surplus monies or idle funds; (3) control such as audits and annual reports; (4) sources of capital financing; (5) public borrowing; and (6) financing from earnings." Id. at p. 15.

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[2] Florestano, Hawk and Lyons. A study of Alcoholic Beverage Control in Montgomery County. Institute for Governmental Service University of Maryland, College Park, Maryland, 1983, p. 9 (citation omitted).

Section 159 established DLC effective July 1, 1951. Paragraph (a) of Section 159 provides that DLC "shall be a department of the County government under the general supervision of the chief administrative officer...." Paragraph (7) of Section 159 provides that the director of DLC shall be appointed by the County Executive with approval of the County Council. The director of DLC serves at the pleasure of the County Executive. In conformance with state law, the Montgomery County Code establishes DLC as a department of the executive branch. Montgomery County Code (1984), as amended, §1A-201(a).

Section 164(e) requires the Department of Finance to keep records of all purchases of alcoholic beverages by DLC, and requires the Department of Finance to forward an annual report to the County Council and the County Executive for the prior fiscal year.

Section 165(e) governs the allocation of profits and reserves of DLC. That section requires all proceeds from the sale of alcoholic beverages to be deposited in Montgomery County banks, to be disbursed by the Director of Finance "in the same manner as other County funds." That section further provides for the allocation of the proceeds from the sale of alcoholic beverages as follows:

> There shall be an adequate balance of working capital within the County's Liquor Control Fund as determined by the Director of the Department of Liquor Control and the Director of Finance and shall be subject to the approval of the County Executive. The amount of the working capital shall be adequate to provide for the continued operation of the dispensary system. The net profits derived from the sale of alcoholic beverages shall be applied in the first instance toward the payment of current interest and retirement charges on such notes, certificates of indebtedness and/or bonds as may be issued by the County Council for the purpose of raising funds for the establishment and operation of the dispensary system. Secondly, the net proceeds shall be applied to the maintenance of adequate working capital. Thirdly, the

balance of the net proceeds shall be deposited as general funds of Montgomery County.

Since DLC is established as a department of the executive branch under state law, with state law requirements for record keeping and allocation of profits and reserves, the establishment of DLC as an authority would require legislative changes to Section 159, and possibly to Sections 164 and 165. The changes in Article 2B would require corresponding changes to §1A-201 of the County Code and §13 of Appendix D of the County Code, which requires all licensees in Montgomery County to purchase their alcoholic beverages from DLC.

In summary, the creation of DLC as an authority or quasi-governmental unit of the County government would require a special act of the state specifying the organizational structure, operational methods, and appropriate powers of the proposed authority.

3. Contracting Out the Operations of DLC

In Ms. Pedersen's memo dated August 2, 1991, she asked whether Article 2B of the Annotated Code of Maryland and/or the County Code would need to be revised to allow DLC to contract out any portion of its operations. Ms. Pedersen set out several options that DLC might consider should this alternative be chosen.

Under state law, DLC has monopoly power over the sale and distribution of alcoholic beverages in Montgomery County. Section 162 provides that "no person, firm, or corporation shall keep for sale any alcoholic beverage not purchased from [DLC]...."

There are no provisions in Article 2B nor in the Montgomery County Code that expressly prohibit DLC from contracting out any portion of its operations. However, DLC would be subject to certain limitations if it contracted out its operations. State law requires that it perform its function as a department of the executive branch exercising monopoly control over the sale and distribution of alcoholic beverages within the County. Under Article 2B all licensees must purchase their alcoholic beverages from DLC, and only DLC may sell liquor package goods for off-premises consumption. These limitations would prohibit a contractor from taking title to the liquor that it sells for DLC. To allow the contractor to assume ownership of the alcoholic beverages it sells to licensees and the public would violate state law.

Moreover, any plan to contract out DLC's operations must be consistent with the general purpose behind the regulation of alcoholic beverages, as set forth in Section 1, which is "to obtain respect and obedience to law and to foster and promote temperance." Allowing private contractors to have profit incentives based on volume of sales might be in conflict with the general purpose behind Article 2B. Therefore, in contracting out its operations, DLC must retain its function of setting policies with respect to pricing, listing/delisting, and promotion.

Finally, as a department of the Montgomery County Government, DLC is subject to the requirements contained in Chapter 11B of the Montgomery County Code, which governs contracts and procurement matters for the County government.[3] DLC is also subject to the Montgomery County Procurement Regulations which have been issued pursuant to Chapter 11B of the Code.

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[3]Chapter 11B of the Code was adopted as directed by Sections 313 and 314 of the County Charter, which require the Council to set up a "centralized system of purchasing and contracting for all goods and services used by the County," and to "prescribe by law for competitive procurement for purchases by or contracts with the County" over certain established amounts. Charter of Montgomery County, Maryland Sections 313 and 314.