

ALCOHOLIC BEVERAGES

**REPORT OF THE
MILITARY MEMBERS OF THE COMMITTEE
TO STUDY THE SALE OF ALCOHOLIC BEVERAGES
AT MILITARY INSTALLATION FACILITIES
to
THE GOVERNOR
and
THE GENERAL ASSEMBLY OF VIRGINIA**



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Department of Purchases and Supply
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HEADQUARTERS FIFTH NAVAL DISTRICT

Norfolk, Virginia 23511

January 20, 1966

Governor Mills E. Godwin, Jr.
Governor of Virginia
Richmond, Virginia

My dear Governor Godwin:

I am enclosing the report of the military members of the Committee which inquired into the sale of alcoholic beverages on military installations in Virginia.

In comparing it with the majority report, I am sure you will observe the broad areas of agreement which all the members of the Committee found. The three military members hope and believe that this supplemental report will be of particular service to you and the members of the General Assembly in pointing up certain areas of the problem which the majority report does not cover with the clarity and candor which we believe the subject deserves.

It has been a privilege and pleasure to work on the Committee in pursuit of a solution to this very important problem of common interest to Virginia and the Armed Forces. As our report relates, we are convinced that the only real solution rests in active and continuing cooperation between the military and Commonwealth authorities. You have our assurance of that cooperation.

Warmest personal regards.

Most sincerely,

E. B. TAYLOR,
Rear Admiral, U. S. Navy.

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THE BACKGROUND

At the 1964 session of the General Assembly of Virginia, two bills were passed relating to the price of beer charged by wholesalers to retail outlets operated by the Armed Forces of the United States on military installations in the Commonwealth of Virginia. The bills were prompted by a growing apprehension on the part of the members of the legislature that a substantial quantity of tax-exempt beer sold to military outlets was finding its way into the hands of civilian consumers who were not entitled to purchase such beer. Beer distributors also expressed concern at certain procurement policies followed by the military authorities in the purchase of this beverage.

Following the adjournment of the General Assembly, the Governor concluded that this legislation was not in the best interests of the Commonwealth, or of the parties concerned, and accordingly vetoed the bills.

The Governor was convinced that through a fair and impartial inquiry the facts could be determined, and the condition which prompted the bills could be alleviated by administrative action on the part of the Commonwealth and the Federal agencies involved.

Accordingly, the Governor appointed a "Committee to make inquiry, and recommendations, if indicated, looking to the correction of any practices that might now exist concerning the procurement and sale of alcoholic beverages to those instrumentalities of government entitled to tax exemption."

This report transmits the views of the military representatives of the Air Force, Army and Navy on the Committee and is forwarded pursuant to our appointment responsibility.

II

THE CRUCIAL ISSUES

The Governor pinpointed the two fundamental areas of controversy, which required further inquiry and evaluation, in his statement of April 3, 1964 concerning the veto of House bills 558 and 677.

One prime area of dissension centered on the accuracy and import of statistics introduced during discussion of these two bills as they were passed through the General Assembly. The Governor addressed himself to this issue in these words:

"I do not believe that any person can consider the available statistics and not question the reason for the astronomical increase in beer sales to instrumentalities of the government entitled to tax exemption as contrasted to the actual decrease in civilian sales."

A second basic controversy stemmed from allegations made by certain Virginia licensed beer distributors that Armed Forces procurement policies were patently unfair and inimical to the efficiency of the law enforcement responsibilities of the Virginia Alcoholic Beverage Control Board. The Governor stated the problem for resolution in this language:

"If it can be determined that procurement policies of the Armed Forces in their purchase of beer from Virginia distributors are frus-

trating or interfering with the controls of the ABC Board over this industry, or are otherwise disruptive—then such policies should be examined and corrected.

Here we should be concerned not with price-fixing, or eliminating competition, but rather with procurement policies or practice which adversely affects the State's control of the alcoholic beverage traffic."

III

EVALUATION OF THE CRUCIAL ISSUES

The results of the intensive and objective search of the entire Committee through several hundred pages of testimony and a great volume of Armed Forces control directives and similar written data is best described in these words of the authors of the majority report, appearing at pages 50 and 51 of that document, to which language we subscribe with qualification.

"Throughout the course of the study we have attempted to determine from all available sources whether or not there is a substantial amount of diversion of tax-free beer into the hands of unauthorized consumers. *While isolated instances have been brought to our attention, we have been unable to determine from any competent evidence that there is a substantial amount of tax-free beer being so diverted.*

We have also carefully considered the information presented by the Department of Defense concerning the number of authorized purchasers living or stationed in Virginia and the information from our State Department of Taxation concerning tax rebates on account of sales to the military, to determine whether an analysis of these figures might substantiate the allegation that large quantities of tax-free beer is being diverted into the hands of unauthorized consumers, to the detriment of the State's revenues. However, after careful analysis we are unable to substantiate such allegations.

It is true that the per capita consumption among the civilian population in Virginia has tended to decline somewhat over the past several years. At the same time the per capita consumption in the military has tended to increase. We feel that there are many factors which must be considered when attempting to determine the cause of such increased consumption on the part of the military. First of all, the military has in the past few years increased both the quantity and the quality of the recreational facilities available to military personnel and other authorized purchasers for their enjoyment and convenience at which tax-free beverages are available. Second, the military population is generally younger than that of the civilian population and their propensity to consume alcoholic beverages incident to their recreational activities is, we believe, probably higher than that of the civilian population, generally. Third, *when all authorized purchasers of tax-free beer are considered as a whole, their total number in relation to that of the adult civilian population in Virginia is not strikingly disproportionate.*" (italics ours)

Thus, on the crucial issue of whether either statistics or specific instances of unauthorized diversion are available to support an allegation of such diversion, seven of the eight members of the Committee are agreed that after some twenty months of intensive search and study there is absolutely no competent evidence in any form, including fact and figure,

which would support the charge of unauthorized diversion of substantial quantities of beer, which has been levied against the military personnel stationed in Virginia. There have been only isolated, unidentifiable and unsupported specific complaints brought to the Committee's attention on the one hand. On the other, the data reflected in pages 25 through 49 of the majority report has substantially supplemented, clarified and corrected the import of the limited statistics appearing on page 10 of that record, which were the only ones available to the Governor at the time he issued his veto statement on April 3, 1964.

We now turn to consideration of the only other major point at issue. This is resolution of the complaints advanced by various Virginia beer distributors that the procurement policies of the Armed Forces are unfair to the individual distributor and detrimental to effective control of the product by the Virginia Alcoholic Beverage Control Board.

A careful review of all procurement directives of the Armed Forces, from the Department of Defense through all lower echelons, make abundantly clear that all are predicated upon sound business management practices, including complete freedom and open competition among suppliers, including all beer distributors in Virginia. These military procurement directives simply and basically require those charged with procurement responsibilities to procure merchandise, including beer, on a competitive basis and at the lowest possible price. Coexistent with this mandate to secure the best price possible in open market competition is the equally forceful requirement that the retail outlet will stock in compliance with customer preferences, subject only to shelf limitations. This limitation does not in any sense constitute a restriction on free competition.

The record makes clear that there is no real disagreement between any of the eight members of the Committee as to the import of the Armed Forces procurement policies. This is amply illustrated by considering the pertinent language in which the report submitted by the other Committee members is couched. It reads as follows, beginning at page 11:

"Exchange procurement is conducted on the basis of full and free competition to the maximum extent practicable and consistent with the immunity of exchanges from State regulation and control. Award is made to the responsible contractor whose offer is most advantageous to the exchange, price and other factors considered. As a matter of policy, exchanges in the continental United States purchase beer from the local wholesaler and deviations are permitted only as authorized by the chief of the exchange service."

The point of disagreement and departure among the Committee members on this score comes in the evaluation of the consequences of the implementation of these Armed Forces policy directives. The line of demarcation is clearly and sharply drawn in considering this language from page 14 of the majority report.

"While the procurement policies and programs of the armed force directed as they are at providing these necessary supplemental services to its personnel and other authorized consumers, are salutary, in and of themselves—particularly from the standpoint of the military. *However, there are inherent disadvantages to the beer wholesalers.*" (italics ours)

This theme of "*disadvantages to the beer wholesalers*" (italics ours) is manifest throughout the entire section of the majority report which deals with the Armed Forces procurement policies. Nowhere in that report is there contained even a hint of serious complication for the Virginia

Alcoholic Beverage Control Board authorities in their efficient enforcement operations relating to the control of the Virginia beer market.

The unvarnished issue, which results from taking a penetrating look at the undisputed facts, comes down to this. Is the ordinary soldier, sailor or airman to be financially penalized because the size of the Armed Forces places them in a favorable competitive position? Or stated from the opposing position, is the individual supplier, the Virginia beer distributor in our situation, so overshadowed in his daily business operations by the economic bludgeon of Armed Forces might that he must have special protection against those Armed Forces in order to avoid individual business disaster?

The answer to these straightforward questions seems obvious to us. The free enterprise system which has made this country great does not coddle any special group. Nor have our modern industrial Goliaths, which thrive on our free enterprise economy, achieved their greatness by such coddling. We find no valid reason for such an extension to the beer industry. Both the Federal anti-trust laws (15 USC 1) and the Virginia restraint of trade statutes (Va. Code 59-20) attest to the validity of this conclusion.

Of one thing we are sure. There has been absolutely nothing developed during the course of the Committee's inquiry which meets the test for improper procurement policies or practice which was laid down by the Governor when he set us to work. His remarks are here repeated from page 4 of this record:

"Here we should be concerned not with price-fixing, or eliminating competition, but rather with procurement policies or practice which adversely affects the State's control of the alcoholic beverage traffic."

IV

ESSENTIAL ANCILLARY FACTS REQUIRING CLARIFICATION

There are several subordinate matters which deserve comment in the interest of accuracy and assuring a complete report for your consideration.

At page 8 of this report it is stated that military retail outlets stock in compliance with customer preferences, subject only to shelf limitations. Further, shelf space and other management practices, such as inventory control, do not pose any restriction on free competition in the procurement of beer by the military retail outlets, whether they sell a substantial or small amount of beer. The statement at page 12 of the majority report on basic stock structure is simply a guideline for Army and Air Force exchanges, which may be exceeded with that Headquarters' approval. As the Committee's statistical data indicates, many of these exchanges carry in excess of 10 brands. Accordingly, the statement at page 16 of the majority report that exchanges "will stock only a few, probably not more than five or six brands in most instances" is grossly in error.

An analysis of pertinent figures developed by the Committee indicates that only 19% of the sales of beer is attributable to Army and Air Force Exchange Service outlets in Virginia. The vast volume, or more exactly 81% of all the sales of beer, comes from the three military services' Club and the Navy Exchange operations, in none of which are there restrictive stocking limitations and in all of which customer demand is the controlling factor.

Accordingly, the guideline of stock limitations, on which the majority report relies in pointing up a procurement pressure potential, has minimal application, if at all, and no real significance.

A second matter requiring additional emphasis is found at pages 17 and 18 of the majority report, where the subject of rebates provided by brewers to wholesalers is discussed. For convenience of reference the language is quoted below:

"In order to gain a competitive advantage, the wholesaler is encouraged by the brewers to grant sizable discounts. To offset the cost effect of such quantity discounts to the wholesaler, in many cases the brewer will rebate to the wholesaler a substantial part of the discount extended to the military. However, this is not true in all cases. Usually only a portion of the discount is rebated by the brewer. Where the brewer does not rebate this discount the burden is borne by the wholesaler...."

We are in general agreement with this statement but believe its further expansion is desirable in order that the fact situation will be accurately understood. First, there were no brewery representatives in attendance before the Committee so it was not possible to fully determine either exact rebate procedures or percentages. Much more important and to the point, however, is the fact, fully supported by the Committee's records, that the rebating is entirely a matter between the breweries and the wholesalers in which the purchasers, that is, the Armed Forces, have absolutely no interest or part. As previously mentioned at page 7 of this report, military procurement is only concerned with buying at the lowest possible price in the open competitive market.

Another facet warranting clarification is the language appearing at pages 52 and 53 of the majority report concerning the relative advantages and disadvantages of the concept of a central military procurement agency. This subject was not explored in depth during the Committee's inquiry and accordingly we are of the opinion that no one should be misled by the observation of the majority report that "its disadvantage to the military would outweigh the advantage to the wholesalers." This is an area of inquiry which, in our opinion, would require substantial additional development before a meaningful evaluation could be made.

Finally, the majority report is silent on one particularly illuminating aspect of this controversy. It fails entirely to mention or differentiate between the marketing situation which applies to the "popular priced" type beers and that of the so called "premium" or "quality" beers. The Committee records are replete with evidence of the fact that it is only in the "popular priced" brands that competition is keen and the Virginia beer distributor is unhappy with his military market. The prices of the "premium" beers remain consistently stable in this military market, with the only appreciable financial benefit accruing to the Armed Forces, both in procurement and retail sale, being reflected in its tax-free status.

This fact brings home the reality of the marketing situation involved, which is simply that there is a fiercely competitive "popular priced" beer market. This is essentially a problem for resolution by the breweries and beer wholesalers within the framework of our system of free enterprise. The fact that the Armed Forces is a large and valued customer should not be permitted to cloud this fundamental precept of both our national and state economy and law.

If there is a problem between the breweries and the Virginia beer wholesalers in which the Commonwealth has an interest, it should, in our

opinion, be resolved through application of the Virginia coercion statute which became law in 1964 (Va. Code 4-80.2) or an amendment thereof, if required to effectively care for the situation.

THE RECOMMENDATIONS

We consider the legislation proposed in Recommendation No. 1 of the majority report to be unnecessary and undesirable for these reasons:

First, there has heretofore been no statutory limitation of any kind on 3.2 type beverages and restrictive legislation should only be added when in the public's best interest.

Second, not one whit of evidence was secured by the Committee throughout the course of some twenty months of search which establishes or even remotely points to the validity of the assertion that there has been any substantial diversion of either 3.2 or high test beer, or any other alcoholic beverages.

Finally, we believe that the proposed legislation imposes an unnecessary and unrealistic, and to that extent undesirable, statutory limitation.

In regard to Recommendation No. 2, which is advanced in the majority report, we have no objection whatever to that aspect of the recommendation which deals clearly and in precise terms with "gifts" in the commonly recognized and generally accepted meaning of that term. Speaking for both the Federal government and the Armed Forces, we welcome all support in elimination of every such practice. Both the Federal Alcohol Administration Act (27 USC 205) and Department of Defense Directive 5500.7 of 17 May 1963 and the implementing directives of the three services bespeak the Federal interest in this area. That it is an active and perceptive interest in Virginia, as elsewhere, is reflected by the concern displayed and enforcement measures implemented here in Virginia in the recent past by both military commanders and the enforcement arm of the Internal Revenue Service of the U. S. Treasury Department. As majority report Conclusion No. 7 indicates, there has been common fault among beer wholesalers and certain Club managers in past years in violation of both laws and regulations relating to gifts. The Armed Forces strongly endorse and lend unqualified support to every effort from any source which is directed toward stamping out this deplorable practice.

It is our opinion, however, that the wording of the proposed legislation goes well beyond this common ground of agreement and seeks to broaden the bona fide "gift" language and concept to the point that it may be so interpreted as to effectively dilute or eliminate free enterprise and the ancillary beneficial requirement of sound business management that the purchaser seek the lowest price for the equivalent product.

The concept of a fixed price, whether established by a state law or a combination of vendors, is contrary to both the laws of the United States and the Commonwealth of Virginia, is similarly contrary to the procurement policies of the Department of Defense and accordingly, is legally objectionable.

Any language which will tend to dilute the concept of a gift by encouraging its application to a situation of fixed price is violative of both Federal and Virginia law and is highly objectionable to the Armed Forces and these representative signatories. We believe the proposed legislation has this fault and to that precise extent find it unpalatable.

VI

CONCLUSION

The members of this Committee have worked objectively and in close harmony over the past many months in wrestling with this complicated and frustrating problem. A careful evaluation of this and the majority report will reflect the broad areas of common agreement. It is our hope that the additional information and comments provided here will further our mutual understanding and provide the basis for future continuing cooperation in the administration and control of this problem of concern to both the Armed Forces and the Commonwealth authorities. We believe that this medium of continuing cooperation offers the only real solution to our mutual quest.

Respectfully submitted,

JOSEPH H. BOTTS

Colonel, GS
Army Representative

HARRY R. BURRELL

Colonel, USAF
Air Force Representative

E. B. TAYLOR

Rear Admiral, USN
Navy Representative

ADDENDUM

Mr. John W. Hardy and Mr. H. E. Bickel, as members of the Committee included evidentiary matters which were not submitted to the Committee as a whole. The military members of the Committee, accordingly, deem it advisable to submit comments of their own in order to bring the following into proper perspective.

Both Mr. Hardy and Mr. Bickel have attached an extract copy of an Army and Air Force Exchange Service Direct Delivery Purchase Order from the Fort Belvoir Exchange to an unidentified Virginia beer whole-

'Seller warrants on the acceptance of this purchase order that the prices and terms set forth herein are at least as favorable as those offered or given to any other retail customer of any type or category without regard to alcoholic content, excluding any state tax.'

This provision has been added to each purchase order directed to every northern Virginia beer wholesaler since the abortive attempt by certain of those wholesalers to fix prices to Army and Air Force exchanges, for which they were subsequently indicted, pleaded "nolo contendere" and were fined. The purpose of such provision is self-explanatory.

In addition both Mr. Hardy and Mr. Bickel have attached a copy of the Virginia Attorney General's opinion of March 25, 1964 to the Honorable Henry E. Howell, Jr. as to the constitutionality of House bills 558 and 677, passed by the General Assembly in 1964 and subsequently vetoed by the Governor.

A careful reading of this opinion will elicit the fact that the Attorney General confined his opinion as to the constitutionality of the named bills to application to all sales to retailers anywhere within the exterior boundaries of Virginia but added that the Paul case left unresolved "any question relative to purchase from nonappropriated funds." Further he said "there is the additional problem of the type of jurisdiction possessed by the Federal government relative to the property on which might be located the various nonappropriated fund activities of the naval and military establishment which purchase beer and 'beverages'."

In the final analysis the Attorney General left open the question of the application of such price-fixing laws to military procurement. At the most he said "there is serious doubt in my opinion that the Paul case has any specific effect on the *general application* of these bills to naval and military installations in Virginia." (*italics ours*)

The military representatives respectfully submit that the Paul case does apply and that, notwithstanding the XXI Amendment to the Constitution, any attempt by the Commonwealth to fix prices of beer or in any way to eliminate competition in military procurement, whether from appropriated or nonappropriated funds, must fail as being in conflict with Federal policy.

Respectfully submitted,

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