

**DEPARTMENT OF PURCHASES AND SUPPLY**  
**REPORT OF THE**  
**VIRGINIA ADVISORY LEGISLATIVE COUNCIL**  
**To**  
**THE GOVERNOR**  
**And**  
**THE GENERAL ASSEMBLY OF VIRGINIA**



HD 7, 1970

**COMMONWEALTH OF VIRGINIA**  
Department of Purchases and Supply

Richmond

1969

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\*Mr. Daniel resigned, August 1, 1969.

\*\*Senator Fenwick, deceased, February 22, 1969.

\*\*\*Mr. Frost, deceased, September 18, 1969.

**DEPARTMENT OF PURCHASES AND SUPPLY**  
REPORT OF THE  
VIRGINIA ADVISORY LEGISLATIVE COUNCIL

Richmond, Virginia  
November 7, 1969

To: HONORABLE MILLS E. GODWIN, JR., *Governor of Virginia*  
and  
THE GENERAL ASSEMBLY OF VIRGINIA

The State of Virginia has maintained a system of centralized purchasing for the benefit of its agencies for the past forty-nine years and for the benefit of its political subdivisions for the past forty-five years. In 1960 this system was expanded with the establishment of a Central Warehouse, which permitted the State to make large purchases of certain supplies at reduced prices for resale to various agencies of the State. In 1964 such resale was authorized to political subdivisions.

Since this latter time, 1964, questions have been raised, especially by certain business interests, of whether the legislative intent and purpose of the present purchasing system have been realized. These questions include: Do the political subdivisions actually save money by purchases from the Central Warehouse? Do the service charges imposed by the Central Warehouse cover all expenses of operations or does the State suffer a loss in providing such services? Does the operation of a Central Warehouse impose an unreasonable restriction on Virginia's economy?

These questions provided sufficient impetus for enactment of House Joint Resolution No. 77 by the 1968 Regular Session of the General Assembly. This resolution is as follows:

HOUSE JOINT RESOLUTION NO. 77

Directing the Virginia Advisory Legislative Council to make a study and report concerning the operation of the Department of Purchases and Supply.

Whereas, in 1920 the State of Virginia initiated a system of centralized purchasing for the benefit of State boards, institutions and agencies and in 1924 expanded the system to permit political subdivisions to seek the assistance of the Purchasing Agent in purchasing supplies; and

Whereas, the purpose of the centralized purchasing agency was to permit such State boards, institutions and agencies and political subdivisions to place orders through one central office in order to take advantage of the lower prices that can be obtained through volume purchases; and

Whereas, from 1920 to 1957, the central purchasing agency fulfilled its original purpose by taking competitive bids on orders placed by the prospective purchasers and awarding contracts to low bidders for delivery of goods directly to the purchaser; and

Whereas, the original purpose of the centralized purchasing office was expanded when the law was amended in 1958 to permit the Director to negotiate bids instead of taking competitive bids and further expanded in 1960 when the Department of Purchases and

Supply was authorized to establish a central warehouse, capitalized with State funds; and

Whereas, since 1960, the Department of Purchases and Supply has purchased delivery vehicles, printed catalogues, employed salesmen and become a large-scale wholesaler of hundreds of items of merchandise; and

Whereas, the General Assembly in 1964 again amended the law to permit the Department of Purchases and Supply to sell and deliver its merchandise from the central warehouse directly to political subdivisions throughout the State; and

Whereas, historically, the Commonwealth has opposed the principle of government competition in areas served by private business and individuals; now, therefore, be it

Resolved, by the House of Delegates, the Senate of Virginia concurring, That the Virginia Advisory Legislative Council is hereby directed to make a study of, and report on, the operation of the Department of Purchases and Supply. Such study shall include, but not be limited to, the effect of the Department's present system of operation upon private business and the economy of the State and its political subdivisions, the cost of its operation to the State, and the practices of other states with respect to centralized purchasing.

All agencies of the State shall assist the Council in its study. The Council shall conclude its study and make its report containing its findings and recommendations to the Governor and the General Assembly not later than November one, nineteen hundred sixty-nine.

Resolved, further, That pending the report of the Council, the operations of the Department of Purchases and Supply should not be expanded beyond their present scope.

The Council selected C. W. Cleaton, South Hill, member of the House of Delegates and of the Council, to be Chairman of the Committee to make the initial study and report to the Council. The following were selected by the Council to serve as members of the Committee: A. E. Berlinghoff, Purchasing Agent of Henrico County, Richmond; L. C. Bird, Member of the Senate of Virginia, Chesterfield County; William E. Black, farmer and member, Mecklenburg County Board of Supervisors, Baskerville; James E. Bowen, Jr., City Manager, Charlottesville; J. H. Daniel, Member of the House of Delegates, Charlotte Court House; Tom Frost, Member of the House of Delegates, Warrenton; J. Wortham Huffman, Retired Purchasing Agent, City of Richmond, Richmond; W. Stirling King, former Mayor of Richmond and Sales Manager of a printing firm, Richmond; Flournoy L. Largent, Jr., Member of the House of Delegates, Winchester; Paul W. Manns, Member of the Senate of Virginia, Bowling Green; W. Roy Smith, Member of the House of Delegates, Petersburg; Dan Stickley, Farm Equipment Dealer, Penn Laird; J. Warren White, Jr., Member of the House of Delegates, Norfolk; and Landon R. Wyatt, Jr., Automobile Dealer, Danville.

At the organizational meeting of the Committee, Mr. W. Roy Smith was elected Vice-Chairman. G. M. Lapsley and John A. Banks, Jr., served as Secretary and Recording Secretary, respectively, to the Committee.

The Committee made a thorough study of the Department of Purchases and Supply, including a review of published material, a tour of the facilities of the State Central Warehouse, briefings by G. Lloyd Nun-

nally, Director, and a management team of the Department, correspondence with all other states regarding their purchase activities, and the holding of a public hearing at Richmond.

The material reviewed included: the 1966-67 Annual Report of the Department of Purchases and Supply, the 1960 Report of the Committee for Economy in Governmental Expenditures, which deals with internal management for the State, Chapter 15 of Title 2.1 of the Code of Virginia, and a special report of the State Auditor requested by the Committee concerning the cost of operating the Central Warehouse.

Replies were received from thirty-five states in response to letters requesting information regarding their purchase activities.

Thirty persons addressed the Committee at its public hearing and fifteen others wrote letters to be incorporated into the hearing record.

The Committee completed its study and made its report to the Council. After thorough consideration and review of these matters, we submit the following:

### RECOMMENDATIONS

(1) That the counties, cities, towns and other political subdivisions be permitted to retain their privilege of purchasing from the Central Warehouse for public use as provided for in § 2.1-288 of the Code of Virginia.

(2) That no restrictions be imposed regarding the rate of service charges for purchases from the Central Warehouse and that the Director, Department of Purchases and Supply, continue to charge a fee for such purchase services at a rate, as best can be determined by him from time to time, that will cover the cost of operation of the Central Warehouse, excluding interest on advancements from the State General Fund.

(3) That the Director, Department of Purchases and Supply, prepare and maintain a Vendor Notification Plan to insure that appropriate merchants within the Commonwealth receive adequate notice of all offers for bids to sell goods they deal in, and that such plan provide that no merchant be deleted from the Department mailing list for such notice until either (1) the merchant has failed to respond to three notices, or (2) the merchant sends written notice to the Department that he does not wish to receive such notices.

### DISCUSSION OF ISSUES

During the Committee's study, many issues were developed which provided a basis for consideration, deliberation and the resultant recommendations. The major issues are as follows: *Are all costs of operating the Central Warehouse accounted for?* A significant number of persons who appeared at the public hearing to speak in opposition to the present purchasing system alleged that all costs of operating the Central Warehouse are not reflected in the Department's annual report and consequently the service charges made for purchases are not sufficient to defray all operational expenses of the Central Warehouse. In cases of purchases by political subdivisions, this would necessarily result in an expense to the State in providing purchase services for these subdivisions and this is not within the legislative intent or purpose of State laws.

In order to evaluate this issue, a subcommittee was appointed to

meet with the State Auditor, Joseph S. James, and members of his staff to request that a report be made by the State Auditor to the Study Committee on all costs of operations of the Central Warehouse and to define the scope of such a report. At that time, the Auditor's office had just completed an annual audit of the Department of Purchases and Supply. Mr. James, in accepting the responsibility for preparing this report, stated that he would be able to show a breakdown of all direct costs to the warehouse with much precision, but that an apportionment of Department overhead expenses must be based on management estimates of the Department's over-all operations.

This report considered operations for the most recent fiscal year, that ended June 30, 1968. In addition to showing a breakdown of all direct costs that are charged to General Warehouse operations, the State Auditor reported what he said "we (his office) feel presents fairly the allocation of costs which should be charged to an operation of this nature, were the policy established to apportion such costs." Such apportioned costs, that are not charged to the Central Warehouse operation in the annual report, are as follows:

#### SALARIES

<i>Position</i>	<i>Salary 1967-1968</i>	<i>Factor</i>	<i>Portion of Salary Allocated for Work on Central Warehouse Matters</i>
Director	\$17,500.00	3.87%	\$ 677.24
Asst. Director	11,846.00	3.87%	458.44
<b>Total Administrative</b>			<b>\$ 1,135.68</b>
Buyer	8,400.00	71%	5,964.00
Clerk-Steno, or Typist C	4,216.00	71%	2,993.36
<b>Total Buying Staff</b>			<b>8,957.36</b>
Clerk-Typist C-Order Writing (156 hours at \$2.08 per hr.)			324.48
<b>Total Salaries</b>			<b>\$10,417.52</b>

#### OTHER COSTS

Office space, including utilities, for Food Buyer and his clerk	\$ 295.71
Telephones for Food Buyer and his clerk	230.04
Retirement and other contributions on compensation	787.50
<b>Total other costs</b>	<b>\$1,313.25</b>

#### TOTAL COSTS

Salaries	\$10,417.52
Other costs	1,313.25
<b>Total costs</b>	<b>\$11,730.77</b>

Had this amount (\$11,730.77) been charged to the Central Warehouse, the net gain of \$11,293.62 for their operations during fiscal year 1968 would have been reduced to a net loss of \$437.15.

Total warehouse sales for the period were \$5,016,773.84, of which \$880,074.94 or 17.54%, was to political subdivisions, and the remainder to State departments, institutions and agencies. If the above net loss of \$437.15 were prorated according to sales, the portion credited to sales to political subdivisions would be \$76.68 for the year, or less than one hundredth of one percent of sales.

*Should the Department be charged for interest on advancements from the State General Fund?* Some persons who spoke at the public hearing contended that since the Department was not charged for interest on advancements from the General Fund, all of the cost of operations were not properly accounted for and, therefore, not as much savings are realized from the departmental operations as one might expect. They further contend that all actual costs should be considered and that interest is a real cost which should be charged to the Department.

The extent of this interest is shown in the following extract of the State Auditor's Report.

During the first six months of the fiscal year, advanced capital amounted to \$1,000,000.00, which was increased in January to \$1,300,000.00. The average month-end advanced capital for the year amounted to \$1,150,000.00. Had interest at 4% (the prevailing rate charged on loans from the treasury) been charged on this average amount, it would have required a charge to operations of the Central Warehouse of \$46,000.00. This amount, however, is without considering the average of the month-end cash balances of \$276,721.61 in the treasury to the credit of the Central Warehouse Fund. Were offsetting interest allowed on this average cash balance, there would be a credit of \$11,068.86, or a net interest requirement of \$34,931.14 for the fiscal period.

Such an interest charge would be approximately seven tenths of one percent of total Central Warehouse sales.

Although advancements from the State General Fund are made to many agencies of the Commonwealth, no charges for interest on such advancements are made against the using agency except in the case of advancements made to the ABC Board. The operations of this Board differ from those of other State agencies since it is proprietary in nature, buying and selling products for resale to the public. Thus, the operation of the ABC Board involves revenue producing activity as well as regulatory functions.

It is felt that it is not within the scope of this study that deals with only one State agency to recommend a change in the established State policy which permits interest-free advancements to virtually all agencies.

*Does the operation of the Central Warehouse reduce purchase costs?* A basic purpose of the Central Warehouse is to reduce purchase costs. Although no specific evidence was found that this objective was not being met, such was suggested at the public hearings.

Letters from several manufacturers and distributors gave evidence that volume purchasing, single delivery point, and the mechanics of order processing employed by the Department result in the lowest possible purchase price. One manufacturing representative stated at the public hearing that his firm sells to the Central Warehouse at a price 20% lower than the price to their distributors. Evidence was also given that localities have saved as much as 19% on their total purchases made from the Central Warehouse.

In considering the feasibility of the Central Warehouse, thought has been given to the additional work which would evolve upon the Department if the Warehouse did not exist. It would appear in such case that approximately 4,765 requisitions would be handled by the Food Buyer as compared with 2,292 at the present time. It has been estimated that it would be necessary to add at least one extra buyer, with accompanying clerical staff, to the payroll of the Department, and it would also become necessary to install an additional order-writing machine. It was estimated by the State Auditor that, based on costs prevailing during the year ending June 30, 1968, an additional cost of \$33,092.84 would be incurred, not including costs of retirement and other fringe benefits paid by the State.

An important service rendered by the Central Warehouse is the delivery of federal surplus commodities to eligible using agencies. During the period covered by the State Auditor's Study, these commodities amounted to 29 rail carloads with a value of \$329,711.25. This has resulted in a substantial saving by eliminating hauling charges and commercial storing expense. The handling of these commodities has been without charge by the Central Warehouse.

*Is adequate notice of all offers for bids being given to all appropriate merchants within the State?* Complaints were made at the public hearing that all automobile dealers were not given a chance to submit bids for automobile purchases by the Department. In one instance, none of the authorized dealers in the county knew about the purchase of automobiles by the Department for that county.

In such a case, it would seem impractical that any retail automobile dealer could make a competitive bid on such purchase since the Department's purchase price is several hundred dollars below the cost to dealers. Regardless of the practical aspect, however, it is felt that all appropriate merchants within the Commonwealth should be given the opportunity to submit bids on all Department low-bid purchases. Therefore, a recommendation is made that the Director establish and maintain a Vendor Notification Plan to accomplish this objective. Each merchant is to remain on the Department's mailing list for such notices until that merchant either fails to respond to three such notices or requests in writing that he not receive such notices.

*Does the present purchasing system adversely affect the economy of the Commonwealth?* In 1965, Dr. George W. Jennings, at that time a Professor of Economics at the University of Richmond and currently a Professor of Economics at Virginia Commonwealth University, conducted an independent study on the Department of Purchases and Supply. Dr. Jennings' major conclusions are as follows:

Because of conditions which appear to be clearly in evidence, the basic conclusion of this study is that the Department of Purchases and Supply, involved as it is in central purchasing and distribution, is operated in the best interests of the citizens of Virginia. Considering all relevant factors together, the Department is actually saving large sums of money for the State and its agencies over and above the cost of its operations.

Under the philosophy of laissez-faire or government-hands-off economics, it is not wise to have the State or any other level of government compete with private business. There is no evidence the State Department of Purchases and Supply is endeavoring to displace private enterprise. It is, however, purchasing and distributing



to provide the best quality commodities at the least cost to government agencies and subdivisions. It is, therefore, in the best interest of the taxpayers of Virginia that the State Department of Purchases and Supply continue to operate essentially as it is now operating.

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General Purchasing and Distribution causes an increase in competition and a shifting of sources of supply from the wholesale distributor to the broker and broker distributor and to the manufacturer. Wholesale distributors tend to be "by-passed" as their functions are no longer necessary. The same condition has happened in the private economy. The number of general line grocery merchants has declined drastically in the past thirty years. This is due to economies of warehousing by chains and cooperative buying. It appears this decline has about ended in Virginia as there was a decline of only one in the years 1958-1963—66 to 65—according to the Census of Business, Wholesale Trade.

The evidence received from the present study leads one to concur with these conclusions.

*Does Virginia's Purchasing System conform with that of other states?* Of the thirty-five other states whose purchase activities were surveyed during this study, only fifteen operate a central warehouse and only two make their warehouse services available to political subdivisions. Twenty of these states, however, make their purchasing services available to their political subdivisions.

Although House Joint Resolution No. 77 directed this study to include practices of other states, it is not felt that such practices should dictate what is the best for this State. Several large distributors, from both Virginia and other states, who do business with several states stated that they feel that Virginia's purchasing system is superior to others; it is a far less complicated way of doing business, and results in better prices. Mr. Albert H. Hall, Executive Vice-President, National Institute of Governmental Purchasers, Incorporated, wrote "The Department of Purchases and Supply of the Commonwealth of Virginia is regarded widely as one of the most efficient and effective public purchasing agencies in the United States."

*Should political subdivisions be permitted to retain their privilege of purchasing from the Central Warehouse?* Many of the major arguments that concern this issue have previously been discussed (savings by subdivisions, cost to the State, effects on the economy, etc.). The remaining major argument against such retention of one of principle—that it is wrong in principle for the State to get involved in the operations and functions of local government.

This, of course, is a philosophical argument that probably could not be completely resolved with any amount of discussion. The main objection concerns control; the opponents resent State interference with local decisions. Since the present laws make local purchases from the Central Warehouse a matter of local option (they can or cannot participate as they wish), these laws do not violate this philosophy. Local governments are a part of the State, and the State has a vital interest in them. Citizens of the localities are also citizens of the Commonwealth, and savings to local taxpayers are savings to State taxpayers.

The terms in the body of House Joint Resolution No. 77, "catalogues", "salesmen" and "delivery", can be misleading. Catalogues are prepared by the Department and issued only to authorized purchasers for the pur-

pose of announcing what is available and not for the purpose of encouraging sales. The Department does not employ any salesmen and, from the evidence of this study, none of their employees engage in activities to stimulate sales. No deliveries are made to political subdivisions except "drop-off" deliveries when Central Warehouse trucks are en route to State agency facilities.

The ability and integrity of the Department staff was never put in issue during this study. Any division of thought was over matters of policy and all comments on the efficiency of operations of the Department were most complimentary.

The Council expresses its thanks to the State Auditor and his office for the report which he submitted to the Committee.

The Council feels that the Department of Purchases and Supply is operated in the best interests of the citizens and taxpayers of the Commonwealth of Virginia.

Our appreciation for the work done by the study Committee should be recorded. Their assistance has been indispensable.

Respectfully submitted,

C. W. Cleaton, Chairman  
J. C. Hutcheson, Vice-Chairman  
Russell M. Carneal  
Robert C. Fitzgerald  
J. D. Hagood  
Edward E. Lane  
Garnett S. Moore  
Lewis A. McMurrin, Jr.  
Sam E. Pope  
Arthur H. Richardson  
William F. Stone  
Edward E. Willey

JAMES M. THOMSON does not concur in this report.



