



Liquor Control System Modernization Study Committee

July 28, 2015

Introduction and Background

- Walk-through of Sec. A.16 of Act 51.
- Overview of the Liquor Control System in Vermont, Maine, and New Hampshire.
- Overview of four reports regarding potential changes to Vermont's Liquor Control System and the Department of Liquor Control.

Enabling Legislation:

Act 51 of 2015, § A.16 (S.138)

- Legislative Charge:
 - “The Committee shall study and evaluate Vermont’s liquor control system and the Department of Liquor Control and determine whether and how the system and the Department can be made more efficient, effective, and profitable for the Vermont economy while protecting the public health and safety.”

Two Specific Areas of Focus

- “...the governance and operation of the Department of Liquor Control...”
- “...Vermont’s regulatory system for the production, sale, warehousing, and distribution of spirits and fortified wines...”

Duties in Relation to the Governance and Operation of the Department

- “(1) examine and evaluate the governance and operation of the Department of Liquor Control, including the manner in which it warehouses and distributes spirits and fortified wines, in comparison with the governance and operation of liquor control agencies in other states, and identify various measures by which the governance and operation of the Department of Liquor Control could be made more efficient, effective, and profitable for the Vermont economy while protecting the public health and safety”

Duties in Relation to the Governance and Operation of the Department

- “(2) examine and evaluate any changes to licensing, enforcement, education, fees, and taxes related to the production, sale, warehousing, and distribution of alcoholic beverages that would be necessary to implement the various measures identified pursuant to subdivision (1) of this subsection”

Duties in Relation to the Governance and Operation of the Department

- “(3) evaluate the impact of the various measures identified pursuant to subdivision (1) of this subsection with respect to:
 - (A) public health and safety;
 - (B) the tax revenue and income generated by the Department;
 - (C) any savings in the cost of the services provided by the Department;
 - (D) any economic impact on the businesses licensed by the Department; and
 - (E) the price and availability of alcoholic beverages for consumers in Vermont.”

Duties in Relation to the Regulatory System for Spirits and Fortified Wines

- “(4) examine and evaluate Vermont’s regulatory system for the production, sale, warehousing, and distribution of spirits and fortified wines in comparison with the systems employed by other states, including systems in which spirits and fortified wines are warehoused or distributed, or both, by private entities, public entities, or a combination of private and public entities”

Duties in Relation to the Regulatory System for Spirits and Fortified Wines

- “(5) identify various measures by which Vermont’s regulatory system for the production, sale, warehousing, and distribution of spirits and fortified wines could be made more efficient, effective, and profitable for the Vermont economy while protecting the public health and safety”

Duties in Relation to the Regulatory System for Spirits and Fortified Wines

- “(6) examine and evaluate any changes to licensing, enforcement, education, fees, and taxes related to the production, sale, warehousing, and distribution of alcoholic beverages that would be necessary to implement the various measures identified pursuant to subdivision (5) of this subsection”

Duties in Relation to the Regulatory System for Spirits and Fortified Wines

- “(7) evaluate the impact of the various measures identified pursuant to subdivision (5) of this subsection with respect to:
 - (A) public health and safety;
 - (B) the tax revenue and income generated by the Department;
 - (C) any savings in the cost of the services provided by the Department;
 - (D) any economic impact on the businesses licensed by the Department; and
 - (E) the price and availability of alcoholic beverages for consumers in Vermont.”

Two Basic Models for State Liquor Control

- The Control Model
 - 17 states are so-called “control states.”
 - All control states directly control the wholesale distribution of spirits within their borders.
 - 13 control states also control the retail sale of spirits through state stores or agency stores.
 - Some control states also control the wholesale distribution or retail sale, or both, of wine.
 - No control states exercise direct control over the sale of beer or the production of alcoholic beverages.

Two Basic Models for State Liquor Control

- Licensing
 - 33 states are licensing states.
 - Licensing states regulate and license private businesses that produce, distribute, and sell alcoholic beverages.

Overview of the Liquor Control System in Vermont

- In Vermont, the Liquor Control Board and the Department of Liquor Control regulate and license the production, distribution, and sale of alcoholic beverages.

Overview of the Liquor Control System in Vermont

- Vermont is a control state.
 - The Department of Liquor Control warehouses and distributes spirits and fortified wines to 80 agency stores for sale to the public.
 - Vermont's agency stores sell spirits and fortified wines on behalf of the Department.
 - Beginning January 1, 2016, the Department will issue permits allowing up to 150 second class licensees to sell fortified wines purchased from the Department.

Overview of the Liquor Control System in Vermont

- Spirits and fortified wines sold by the Department of Liquor Control are subject to a 25% excise tax.
- In FY 2014, the Department of Liquor Control generated \$22,930,797 in revenue for the General Fund.

Overview of the Liquor Control System in Maine

- In Maine, the Bureau of Alcoholic Beverages and Lottery Operations and the Maine Liquor and Lottery Commission license and regulate the manufacture, distribution, and sale of alcoholic beverages.

Overview of the Liquor Control System in Maine

- Maine is a control state.
 - Maine has approximately 485 agency stores that sell spirits for off-premises consumption.
 - The Bureau determines the listing and pricing of spirits with the assistance of the Commission.

Overview of the Liquor Control System in Maine

- Warehousing and distribution are accomplished through a public-private partnership.
 - Following a competitive bid process, in 2004, Maine signed a 10 year contract to lease its spirits business to Maine Beverage Company for 10 years for an up front payment of \$125,000,000 and annual profit sharing.
 - Beginning July 1, 2014, Maine entered a new 10 year contract with Pine State Spirits to warehouse, distribute, administer, and market spirits on behalf of the State.

Overview of the Liquor Control System in Maine

- According to National Alcohol Beverage Control Association, the sale of spirits generated \$9,971,800 in revenue for Maine's General Fund in 2013.

Overview of Liquor Control System in New Hampshire

- In New Hampshire, the New Hampshire Liquor Commission licenses and regulates the manufacture, distribution, and sale of alcoholic beverages.

Overview of Liquor Control System in New Hampshire

- New Hampshire is a control state.
 - Liquor and wine are warehoused at and distributed from two state warehouses.
 - One of the warehouses, located in Bow, NH, is operated by a private firm pursuant to a contract with the State.
 - New Hampshire operates 77 State liquor and wine outlets.
 - Wine is also sold by licensed retailers.

Overview of Liquor Control System in New Hampshire

- New Hampshire does not tax the sale of wine and spirits.
- The New Hampshire Liquor Commission contributed approximately \$148,600,000 to the New Hampshire General Fund in FY 2014.

Studies of Potential Changes to Vermont's Liquor Control System

- At least four reports regarding potential changes to Vermont's Liquor Control System have been prepared since 1994.
 - A 1994 report prepared by Legislative Council.
 - A 2005 report prepared by Management Analysis, Inc.
 - A 2011 report prepared by the Department of Liquor Control.
 - 2014 report prepared by the State Auditor.

The 1994 Legislative Council Report

- Prepared by the Office of Legislative Council for Representatives Karen Kitzmiller and Michael Obuchowski.
- The report addressed two issues:
 - Whether the existing Vermont liquor control operations were reasonably efficient.
 - Whether Vermont could achieve revenue gains by privatizing all or part of Vermont's liquor monopoly.

The 1994 Legislative Council Report

- Summary of Findings:
 - Both partial- and full-privatization would be unreasonable for Vermont because expected increases in liquor prices would cause sales to be lost to adjacent states, which, in turn, would reduce State revenues from the sale of spirits.
 - The Department of Liquor Control appeared to be relatively efficient, but could realize additional savings by completing the transition from State liquor stores to agency stores.

The 2005 M.A.I. Report

- Prepared by Management Analysis, Inc. (M.A.I.) for the Secretary of Administration pursuant to Act 122 of 2004, § 76a.
- The report examined whether the Department's purchasing, transportation, warehousing, and wholesale distribution functions could be handled more cost-effectively through alternative delivery systems.

The 2005 M.A.I. Report

- Summary of Findings
 - Contracting out for the Department's purchasing, warehousing, and distribution functions via a traditional service contract would not provide sufficient savings to be warranted.
 - Under 3 V.S.A. § 343, a function performed by State employees cannot be contracted out unless it would result in at least a 10% cost reduction.

The 2005 M.A.I. Report

- Summary of Findings continued
 - Selling the rights to the Department's purchasing, warehousing, and distribution functions, similar to Maine, is not recommended because it would likely result in less revenue for the State than continued in-house operation.
 - Recommended continuing in-house performance of the Department's purchasing, warehousing, and distribution functions and implementation of specific operational improvements.

The 2011 Department of Liquor Control Report

- Prepared by the Department of Liquor Control pursuant to Act 146 of 2010, § B.6.
- Report addressed increasing General Fund revenue through innovative changes in the administration of sales of alcoholic beverages.
- The report recommended 9 options for increasing General Fund revenue.

The 2011 Department of Liquor Control Report

- Summary of Recommendations:
 - Create a gift card program.
 - Make specific improvements to the Best Buys and Prime Focus sales programs.
 - Continue marketing efforts with emphasis on magazines, on-line customer lists, out-of-state advertising, on-line special orders, expanding number of liquor outlets, and promoting in-State distilleries.

The 2011 Department of Liquor Control Report

- Summary of Recommendations:
 - Expand the Department’s website with an emphasis on retail to reflect marketing objectives.
 - Examine various changes to the pricing and taxation of spirits including:
 - Maintaining the existing tax and focusing on pricing of categories where most profit can be realized.
 - Switching to a per gallon tax structure.
 - Substituting a flat or flexible markup for the current tax.
 - Hiring an independent consultant to analyze the issue.

The 2011 Department of Liquor Control Report

- Summary of Recommendations:
 - Consider setting a \$15,000,000 annual amount of revenue paid to the General Fund, and distributing additional revenue to the Department to pay for IT and warehousing improvements as recommended by the MAI Study.

The 2014 Report of the State Auditor

- Prepared by the Office of the State Auditor.
 - Two objectives:
 - To assess the fiscal impact of privatizing Vermont's liquor control system.
 - To assess whether the profitability of Vermont's current liquor control system can be improved.

The 2014 Report of the State Auditor

- Summary of Findings:
 - Under models for both full- and partial-privatization, sufficient revenues would be generated to both cover the cost of operating the Department and match the existing operation's projected payments to the General Fund in FY 2016.
 - “The full and partial privatization financial models incorporate an assumed increase to the existing excise tax rate as well as reduced cost of operations for [the Department].”

The 2014 Report of the State Auditor

- Summary of Findings:
 - “[The Department] may improve profitability by conducting analyses to inform strategic decisions and enhancing mechanisms it uses to manage day-to-day liquor operations.”

The 2014 Report of the State Auditor

- Summary of Recommendations:
 - “Although we estimate that a neutral fiscal impact may be achieved from privatization, we make no recommendation to alter the current liquor control system.”
 - Recommends 10 actions to enhance the Department’s profitability by improving strategic and business analysis, warehouse operations, agency store performance, and the effectiveness of sales promotions.



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