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ELIMINATE UNIFORM SELLING PRICE OF SPIRITS FOR OFF- PREMISE CONSUMPTION

House Bill 4458 (Substitute H-2)
First Analysis (10-16-03)

Sponsor: Rep. Sal Rocca
Committee: Regulatory Reform

THE APPARENT PROBLEM:

Retail prices of bottled liquor, or spirits, are established by the Liquor Control Commission. Under the Liquor Control Code, generally speaking, the LCC establishes the prices consumers must pay for a bottle of alcoholic liquor for consumption off the premises by applying a state markup to the cost of the product to the state, and adding a series of specific taxes. The markup, or gross profit to the LCC, is set in statute at not less than 51 percent and not greater than 65 percent. The current actual markup is 65 percent. (When the product is sold to retailers a discount of 17 percent is applied to the marked-up price. See Background Information.) Spirits sold for consumption on the premises can be sold at any price above the cost to the retailer, while spirits sold for off-premise consumption must be sold at the uniform retail price set by the LCC.

Off-premise liquor licensees - which include grocery stores, drugstores, and package liquor stores - say that in recent years they have faced increased financial pressure, largely due to increased competition and increased costs in employee wages, business-related goods, and other expenses. Over the years, there have been a number of bills introduced designed to help licensees address some of these cost increases. Most of the legislation, including the introduced version of this bill, called for an increase in the discount provided to licensees when they purchase liquor from the state. However, an increase in the retailer discount, unless accompanied by a proportionate increase in the markup (and higher liquor prices) has a negative fiscal impact on the state. The original version of House Bill 4485, which would have increased the discount from 17 percent to 20 percent, for example, was estimated to decrease state revenue by over \$20 million. Given the fiscal realities facing the state, increasing the discount to retailers does not seem prudent at this time. As a result, industry representatives have sought ways to deal with their ever-increasing costs without significantly reducing the state's financial fortunes.

One suggested solution is to permit off-premise liquor licensees to sell liquor at a price above the price set by the Liquor Control Commission. This could provide the same benefit of to retailers as increasing the discount but without the negative impact on the state budget.

THE CONTENT OF THE BILL:

The bill would amend the Liquor Control Act to permit alcoholic liquor sold by off-premise retailers (a licensed specially designated distributor or SDD) to be sold at a price equal to or greater than the minimum retail selling price fixed by the Liquor Control Commission. (Alcoholic liquor could not be sold below the minimum retail selling price.) "Retail selling price" would be defined to mean the sum of the price the commission pays for the spirits and the gross profit established by section 233 (that is, the state markup). The bill would also specify that the retail selling price would also be the base on which specific taxes on the sale of liquor are levied. (This means the specific taxes would not be levied on a price higher than the state-determined retail price, even if the retailer charged a higher price.)

MCL 436.1229

BACKGROUND INFORMATION:

There are four taxes that are levied on the price of the liquor after the markup. These include a four percent excise tax for the School Aid Fund, a four percent specific tax for the General Fund, four percent tax for the Convention Facility Development Fund, and a 1.85 percent specific tax for the Liquor Purchase Revolving Fund. The specific tax for the Liquor Purchase Revolving Fund is only levied on the retail selling price of spirits for consumption off the premises of a licensee. The six percent state sales tax is levied on the retail selling price plus the specific taxes.

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The following is a simplified example of how the cost to the consumer is determined for spirits sold for consumption off the premises.

- The LCC purchases a bottle of spirits at \$6.06.
- The LCC applies a 65 percent markup, establishing a retail selling price of \$10.
- The retailer purchases the product at a 17 percent discount from the retail selling price (\$8.30).
- Four specific taxes totaling 13.85 percent are added to the \$10 retail selling price (\$11.385).
- The price to the customer is the retail selling price, plus the specific taxes, plus the six percent state sales tax (\$12.07).

FISCAL IMPLICATIONS:

According to the House Fiscal Agency, the fiscal implications are indeterminate. (10-16-03)

ARGUMENTS:

For:

Supporters say the bill is necessary because, as stated above, off-premise liquor licensees are facing, and have been facing for quite sometime, increases in their business costs. Licensees include businesses of all shapes and sizes, from small independent, neighborhood liquor stores and grocery stores to national and regional “super centers.” These types of stores, in general, don’t operate with a significant profit margin, and when faced with increases in costs and competition, find that limited profitability further eroded. As a result, retailers must either increase costs of other items (which make it difficult to compete with other retailers) or reduce their expenditures (including reductions in employment).

It should also be noted that while both the state and spirits manufacturers can increase their prices under current law, retailers are not afforded the same opportunity. In lean economic times such as this, manufacturers have increased the selling price of their product to the state. The state has also increased its markup on several occasions when selling liquor to licensed retailers. The bill, then, provides retailers with the same opportunity to increase their profits when the need arises, within traditional market constraints.

Further, current law only requires off-premise retailers to sell liquor at the uniform price set by the

LCC. On-premise retailers, by comparison, are permitted to sell liquor by the glass at any price. The bill grants off-premise retailers the same flexibility already afforded to on-premise retailers to set their selling prices consistent with market demand and competitive pressures.

Response:

The bill represents a significant departure from longstanding state practice regarding the pricing of spirits sold for off-premises consumption. While the bill would not allow spirits to be sold below the state-established retail selling price (as a “loss leader”), it does allow for prices above that level. This could lead to price gouging in areas where there is not much competition.

POSITIONS:

The Liquor Control Commission is neutral on the bill. (10-15-03)

The Associated Food Dealers of Michigan supports the bill. (10-14-03)

The Michigan Grocers Association supports the bill. (10-14-03)

The Michigan Beer and Wine Wholesalers Association supports the bill. (10-14-03)

Analyst: M. Wolf

■ This analysis was prepared by nonpartisan House staff for use by House members in their deliberations, and does not constitute an official statement of legislative intent.