Senate Fiscal Agency
P. O. Box 30036
Lansing, Michigan 48909-7536

BILL ANALYSIS

Telephone: (517) 373-5383
Fax: (517) 373-1986
TDD: (517) 373-0543

House Bill 4458 (Substitute H-2 as reported without amendment)
Sponsor: Representative Sal Rocca
House Committee: Regulatory Reform
Senate Committee: Economic Development, Small Business and Regulatory Reform

Date Completed: 11-9-04

RATIONALE

In Michigan restaurants and bars, the price of cocktails varies from establishment to establishment, but the price of each bottle of spirits in grocery stores, drug and convenience stores, and package liquor markets remains constant from store to store. This is because, under Michigan law, liquor for "on premises consumption" may be sold at a price above the cost to the retailer, but liquor for "off premises consumption" must be sold at a uniform retail price set by the State Liquor Control Commission (LCC). According to the LCC, the State established the system of uniform retail pricing shortly after the repeal of Prohibition in an attempt to regulate carefully the manufacture, distribution, and sale of liquor.

Under the Michigan Liquor Control Code, the State acts as the liquor wholesaler: The Liquor Control Commission purchases bottled spirits from suppliers and marks it up for profit to the State. (The Code allows the Commission to establish a gross profit of from 51% to 65% added to the price it pays for spirits. The Commission currently maintains a 65% gross profit.) The LCC then discounts this amount by 17% and sells the product to licensed retailers. Retailers must charge this price, plus State taxes, to their customers. Many retailers would like the opportunity to make a greater profit on the sale of liquor, particularly if their business is seasonal, or if they experience increased costs in wages, insurance, utilities, and rent. In the past, retailers have asked for a greater discount from the LCC; however, this would mean a decrease in revenue for the State, which, due to the current budget situation, is not considered feasible. It has been suggested that retailers be allowed to sell bottled liquor at a price above that established by the Commission.

CONTENT

The bill would amend the Michigan Liquor Control Code to allow specially designated distributors (SDDs) to sell alcoholic liquor at a price equal to or greater than the minimum retail selling price fixed by the Liquor Control Commission. The bill specifies that liquor could not be sold at less than the minimum retail selling price. Currently, liquor sold by SDDs must be sold at a price fixed by the Commission. (An SDD is a person licensed by the Commission to sell packaged liquor for off-premises consumption.)

The bill would define "retail selling price" as the price the Commission pays for spirits plus the gross profit established in the Code. This definition also would apply to sections of the Code providing for specific taxes, which are percentages of the retail selling price.

The bill would define "minimum retail selling price" as the retail selling price plus the specific taxes imposed on liquor in the Code.

MCL 436.1229

ARGUMENTS

(Please note: The arguments contained in this analysis originate from sources outside the Senate Fiscal Agency. The Senate Fiscal Agency neither supports nor opposes legislation.)

Supporting Argument

Permitting retailers to mark up the cost of liquor would give business owners more flexibility and options when business flags or costs escalate. For example, some retailers are located in tourist destinations that are busy just a few months of the year. A retailer could increase the price of liquor during the tourist season but mark it down again when business dies down; or vice versa, depending on what the market supported. Since retailers would not be allowed to mark liquor prices *below* the price set by the LCC, the bill would not encourage greater alcohol consumption. Instead, the bill would allow retailers to experiment with higher prices to try to offset some of the rising costs of running a business. The State would not see a loss on its end, either. If retailers and the State could benefit, and consumers would not be harmed, it would make sense to loosen up some of Michigan's stiff control on liquor pricing.

Legislative Analyst: Claire Layman

FISCAL IMPACT

The bill would have a fiscal impact on State revenue, depending upon how price variations would affect the amount of liquor purchased. If consumption remained the same, and were completely unresponsive to any price increase that would occur under the bill, the bill could generate additional sales tax revenue. However, if consumption declined in response to the price increases, either through the purchase of less expensive liquor or due to reduced consumption of liquor, revenue to the School Aid Fund and the General Fund would be adjusted accordingly.

For example, inclusive of the Liquor Control Commission's 65% markup, $794.2 million of liquor is expected to be sold in Michigan during FY 2004-05. If the bill resulted in an average increase in liquor prices of 10%, using a common assumed measure of price responsiveness, sales would decline by 5%. Net sales would be higher, at $829.9 million. However, the distribution of revenue would be changed.

Retailers receive revenue through a set percentage of the price set by the Commission, referred to as the discount. The discount comprises 17% of the price set by the Commission, not the retail price. In this example, if sales declined 5%, the discount would decline approximately $6.8 million. The amount of the markup received by the State would similarly decline by $8.9 million.

Liquor taxes and the sales tax are levied on the retail price of the liquor. Because the retail price would be higher under the bill, revenue under these taxes would increase. In this

example, sales tax revenue would rise by approximately $2.1 million, and would be split among the General Fund, the School Aid Fund, and revenue sharing. In the example, liquor tax revenue would decrease by $5.5 million, and the decrease would be distributed across the General Fund, the School Aid Fund, the Convention Facilities Fund, and the Liquor Purchasing Revolving Fund.

The net effect of all of these changes, is summarized in the following table.

Distribution of Revenue Effects of a 10% Liquor Price Increase
Net Effect of Changes, with State Impact By Fund
(dollars in millions)

Fund	**Fiscal Impact**
General Fund	-$10.4
School Aid Fund	$0.0
Conv. Facilities Fund	-$1.6
Liquor Purch. Revolving Fund	$0.7
Revenue Sharing	$0.5
Liquor Retailers	$33.0

To the extent that prices would increase by more or less than the amount assumed in the example, the actual impact of the bill would be different. Generally, higher price increases would make the increases in revenue higher and the losses in revenue (to the General Fund) greater. Similarly, smaller price increases would reduce both the losses and gains to each fund or entity receiving liquor revenue.

This analysis is preliminary and will be revised as new information becomes available.

Fiscal Analyst: Jay Wortley
David Zin

H0304\s4458a