KANSAS ASSOCIATION OF BEVERAGE RETAILERS

We are Kansans working for Kansas.

February 4, 2013

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Kansas Licensed Business

"It is a privilege, not a right, to have a Kansas Liquor License. The responsibilities of selling this highly regulated product were made clear to me when I invested in this business. It is according to this agreement – this contract with the State of Kansas that I have invested in the liquor store business and maintained those obligations in good faith."

"Shouldn't Kansas honor my investment by maintaining a stable and reliable business environment – instead of changing the rules mid-stream?"

Dennison Woods, Ken-Mar Liquor, Wichita

The Free Market

Kansas must offer a reliable and stable regulatory environment to encourage investment and growth.

No State operates a Free Market for the sale of alcoholic liquor

- No other state operates the deregulation system proposed by Uncork Kansas.
- Even the Missouri model offers more regulation – with local licensing in addition to state licensing.
- Many of the states that allow alcoholic liquor to be sold in the corporate chain model are “control” states with contract relationships and a variety of restrictions.
- States that are not control states, but do allow similar deregulation utilize other limitations such as limiting the number of off premise licenses on either a statewide or local regulatory framework and using local regulatory licensing boards.
- Example: New Mexico – allows grocery sales of alcoholic liquor but limits the total number of liquor licenses to 1000 for the entire state. This license is for on premise or off premise sales of beer, wine and spirits. Other types of on premise licenses are newly available.

Liquor should not be sold like bread and milk.

- The Hall study makes the assessment that grocery retail models are better than liquor stores and that grocery retail jobs are better than liquor stores. Not true. See Review.
- “Prohibition era” laws regulate the sale of alcoholic liquor products in every state, since virtually all states made the decision about how the products would be sold around the time of repeal.
- The most recent deregulation changes to retail sales systems involve states going from control states to private retail states. Kansas IS ALREADY a private retail state.
- There is no trend of states deregulating private retail markets.

Contents of HB 2532 in 2012

Based on original SB 54 from 2011 – without most of the Senate Committee amendments

- Creates new licenses: Class A for Strong Beer and Class B for Strong Beer and Wine – allowing 18 year olds to sell these products.
- Allows corporations to own liquor stores
- Allows chain liquor stores
- Removes the Kansas residency requirement to get a license and U.S. citizenship requirements
- Allows the business to sell other products
- Would require employees 18 years of age to sell alcoholic liquor – but doesn't state how that would be regulated. (Does not define "sell".)
- Repeals K.S.A. 41-103 – which requires the separate sale of 3.2 cereal malt beverages , creating a duplicate licensing system for retailers who choose to sell strong beer and cereal malt beverage products. Needs some specific direction for the prioritization of regulatory authority.
- Repeals part of K.S.A. 41-308 – which prohibits a retail liquor store from giving away things of value, as well as the prohibition against entertainment, pinball machines, or games of skill or chance. It appears the rest of the statute is retained by New Section 2.

- Class C licenses – for selling beer, wine and spirits - are temporarily capped at current levels – 760 today – and open to all in 2016.

Exempts corporate owners of less than 25% ownership from the majority of license requirements, including U.S. residency, felony convictions, having to be 21 years of age, etc.*

- Removes the requirement that corporations authorize the Secretary of State to accept service of process for out of state corporations.

- Allows corporations to have a retailers license, but exempts them from all the license prohibitions of K.S.A. 41-311 and K.S.A. 41-311(b): requiring U.S. citizenship, Kansas residency, requiring that the owner be 21 years of age, no felony convictions, no former liquor or cmb license revocations, no convictions or bond forfeiture relating prostitution, no convictions or bond forfeiture relating to illegal gambling business or crimes opposed to decency and morality, law enforcement officers or supervisors, holding a cmb license, requiring ownership or a lease for the licensed property, spouse requirements, etc. Except that the section regarding beneficial interest other liquor businesses is retained. Out of state corporations would have to have a registered agent in Kansas and would be subject to Kansas jurisdiction.

Free Markets and Alcohol are a bad mix

Illustration: Brazil

No Business Regulation

- High homicide rate (27 per 100,000 pop. V. 5.7 for United States)
- Estimated 50% alcohol involvement in traffic fatalities v. 32% for United States.
- Liver cirrhosis rate is 11.31 V. 7.47 for US.

Price is Brazil's number one problem for preventing abuse

- Milk = 60 cents (1 liter)
- Mineral Water = 40 cents/ltr
- Big Mac = $1.30
- Beer = 25 cents (1 can)
- Cachaca – 50 cents (1 liter)

(Source: Why can't we sell alcohol like tires and mayonnaise? Pamela S. Erickson, Public Action Management, PLC)

Deregulation and alcohol don’t mix

Illustration: Great Britain

24-hour sales allowed in pubs and stores.

Price controls, bans on volume discounts do not exist

Large retail grocers sell alcohol below cost

Drinking-related deaths doubled between 1991 and 2004 for 15-34 year olds (Office for National Statistics)

Liver cirrhosis deaths for men increased in England and Wales from 8.3 per 100,000 in 1987 to 17.5 in 2002.

(Source: Why can’t we sell alcohol like tires and mayonnaise? Pamela S. Erickson, Public Action Management, PLC)

Contents of HB 2532

Includes:

- Requires new licensee to be a grocery or convenience store (or liquor) – using a broad definition that will include additional businesses not currently contemplated by ABC estimates.
- Includes background requirements for corporate applicants owning more than 25%, this is a significantly lesser standard than currently required for other corporate licensees in the Liquor Control Act that sell to the public (such as Drinking Establishments)
- Removes the 21 years of age requirement for employees and substitutes a minimum 18 years of age “to sell at retail any alcoholic liquor at the point of sale”.
- Prohibits authorizing or allowing a convicted felon “to sell at retail any alcoholic liquor at the point of sale”.
- Continues to provide un-level playing field in terms of enforcement / different penalties
- No real acknowledgement of the negative impact on investments

The Myth of the Moratorium

No legitimate license cap in HB 2532 – a temporary cap simply slows the decline of value.

1. Anyone could get a strong beer and/or wine license (Class A or Class B) immediately. Grocery stores have indicated these are top priority products. These are the products on which licensed liquor stores base their businesses.
2. There is no reason to assume any of the corporations wanting to enter the smaller spirits market will not wait 3 years to buy a license.
3. This does not create value for rural liquor stores licenses. These communities are dominated by big box out of state entities that will wait patiently for 3 years.
4. County restriction on buying licenses provides little or no protection for current successful businesses.

As SB 54 was amended by the Senate committee last session, there is only one license for all alcoholic liquor – beer, wine and spirits. However, it still has an end to the cap on licenses – a cliff where all liquor store owners will see the value of their business plummet.

Licensees do not "own" their liquor license, and the license is attached to the property – does not travel with the licensee.

Any numeric limitation on the number of years places the negotiating advantage squarely in the hands of the new entities.

Although advertised as an opportunity to "transition to a new business model" – the amended bill does not allow liquor stores to change their business model during the moratorium.

Proliferation of Licenses

- Alcoholic Liquor = Strong Beer, Wine & Spirits
- Immediately more than triples the number of strong beer and wine outlets based simply on the number of cereal malt beverage licensees today.
- Possible addition of 2000 to 3000 outlets – then reduced by numbers of independent liquor stores to cease business. Estimates based on three separate related studies indicate anywhere from around 1/3 to ½ of stores would be likely to fail.
- Duplication = Could retailers hold liquor licenses and cmb licenses under this system? What is the interaction of the regulatory systems? For instance = cmb retailers currently sell on Christmas and Thanksgiving.

2008 DISCUS Analysis of Strong Beer Impact

- *"Currently, the 726 package stores allowed to sell full strength beer sell an estimated 17,600 cases per year. Accounting for both the new beer volumes and the new number of full strength beer licenses, the average number of cases sold per outlet will decline to around 4,480 cases per year.'*
- *For the new full strength beer licensees, most of the new volume will be incremental (except that volume which is replacing 3.2 beer sales). Thus, grocery and convenience stores will be able to sell comparatively low volumes of .. beer profitably. Obviously, this does not preclude large supermarkets from selling tremendous volumes. What it does mean, however, is that the 3,790 convenience and grocery stores in the state will be able to take sales away from traditional package stores."*
- *"Accounting for both the lost spirits sales and lost beer sales, total package store revenues would decline from $461.3 million to $254.6 million – a 45% reduction."*
- *"Clearly, not all businesses could withstand a 46% decline in revenues. As a result, we would expect a decline in the number of package stores."*
  "The $254.6 million in total package sales would support a total of 509 package stores. Thus, 217 package stores are projected to go out of business. Naturally, as the number of package stores declines, the availability of spirits will decline as well."
- *(The analysis relies on Kansas sales statistics, market analysis by Gallup Organization, Sept. 29, 2006; and tax receipts by the Kansas Department of Revenue.)*

Colorado Economic Impact Assessment by Summit Economics, LLC, 2009

- *"The Colorado Liquor Stores will lose 50 percent of full-strength beer sales to supermarkets and convenience stores in the first year alone. They will lose 70 percent of beer sales within 3 to 5 years. It is estimated that 40 percent or 700 of the stores will be forced to close within the first 3 years. This will result in the loss of 4,830 wage and self-employment jobs. Overall the Colorado Liquor Stores will lose $700 million in annual revenues, resulting in a permanent $90 million loss in annual wages and proprietor income earnings. These losses will continue through the fifth year. After the fifth year the new market structure will stabilize with 900 fewer stores. There will be 5,500 fewer jobs in the industry, resulting in a loss of $120 million annually in employee and proprietor earnings."*

Review of Economic Study

The full Review explains in Section 1 why the Study's methodologies cannot be expected to arrive at credible estimates. Section 2 describes a major error in the Study's analysis of the productivity effect. Section 3 describes the unlikely nature of the Study's estimates of construction effects. Section 4 describes a problem in the Study's analysis of multiplier effects. Section 5 lists several other methodological errors, questionable assumptions, and overstated arguments, without giving a full analysis.

February 5, 2011

Executive Summary

- ♦ *If there are significant productivity benefits to be had in retailing, they are almost surely orders of magnitude smaller than what the Study has estimated.*
- ♦ *The rather prodigious amounts of construction benefits depend entirely on the model discredited in Section 2, and hence are not to be believed.*
- ♦ *The IMPLAN model utilized by the Study makes a default assumption that changes in the government's revenues are exactly matched by changes in its expenditures, so that increases in economic activity have no net impact on the budget. In that case these changes would not help address the Kansas budget problem.*
- ♦ *The Study focuses on the benefits of regulatory change and ignores most of the costs.*
- *The Study suggests that relaxed regulations could slow down or reverse the historic trend of retailing to abandon sparsely developed rural areas in favor of more centralized retailing in areas with denser development. Actually, standard theory suggests that the opposite is much more likely, i.e. that rural abandonment will be speeded up. In particular, rural abandonment is driven, among other factors, by improved transportation combined with the rise of larger and larger retailing units run by chain—i.e. supermarkets and Wal-Marts—plus the rise of high-volume convenience stores, also run by chains. … Deregulation will achieve productivity gains only to the extent that it adds to these forces. Hence deregulation is likely to speed up the centralization of retailing away from small, scattered, rural sole proprietorships and towards centralized chains.*
- ♦ *The Study fails to consider the potentially negative impacts on the state economy of shifts from locally owned enterprises to national chains.*

David Burress has an M.A. in Physics and a Ph.D. in economics from the University of Wisconsin-Madison. He worked for 20 years as a research economist in the Institute for Public Policy and Business Research at the University of Kansas. Much of his research focused on the Kansas economy using input-output modeling, regional impact analysis, business location theory, and state and local taxation theory, generally in cooperation with KTEC or Kansas, Inc. He also studied the Kansas and national impacts of technology development. He has testified to committees of the Kansas legislature on tax policy, retail wheeling of electricity, economic development, and other topics. He served on Governor Joan Finney's blue ribbon tax reform committee. Burress also served as a Lawrence-Douglas County planning commissioner for six years, where he benefitted from a close-up view of economic development. After retiring from KU he helped found Ad Astra Institute.

The COST

- Sales Tax Reduction
- State Highway Fund FY 12 (-$250,000)
- State Highway Fund FY 13 (-$500,000)
- State General Fund = 3% of $54 m = transfer to city/county each year (offset?)
- $1,654,564 FY 12 estimated cost for SB 54
- Of this, approximately $1.4 m was ongoing for FY 14 and on for 20 FTEs

The Cross Border War

In spite of the stories you hear, customers do not go to Missouri to buy liquor products because the wine is sitting on the shelf next to the cheese and fruit.

Missouri taxes are lower on food, fuel, tobacco and liquor. This bill will not change that.

Missouri consumption rates are not significantly higher than Kansas.

Level Playing Field

- Enforcement – license the whole premises = whole premises suspension
- Purchasing power – big box and grocery stores have the benefit of space and volume. This gives them an advantage relating to purchasing during sale periods and access to allocated products.

"The proponents of this bill talk about level playing fields and say that liquor stores are "protected" by Kansas law. Last year, they even called liquor stores – who, by the way, are in direct competition with each other – a "monopoly". This shows a lack of understanding in the Kansas retail liquor licensing system, which is already privatized and encourages competition. Even the cities can't limit the number of liquor licenses issued in their borders.

In Manhattan, there has been a huge controversy about the downtown development project that helped to bring a Hy-Vee to our town. That project involved the city using eminent domain for the property, getting approval for the State of Kansas and the City of Manhattan to issue STAR bonds for public portions of the development, and using Tax Increment Financing for building the retail development. Tax Increment Financing means that the sales tax collected at the store is used to pay off the costs of the building project instead of going into the city and county sales tax fund or the State General Fund. Of course, at that time, Hy-Vee wasn't going to be allowed to sell liquor. Can you imagine that Kansans would ever support using public funding to build a liquor store? Is this the free market they are talking about?"   Michael Towne, The Library, Manhattan

What about Beer and Wine?

- Beer and Wine are defined in statute as alcoholic liquor.
- Many states that do allow strong beer or wine to be sold through corporate outlets have restrictions on alcohol content for the wine and the beer that can be sold.
- Every alcohol product is defined by alcohol content – whether the product is made from fruit or grain is irrelevant.
- Regardless of how often the lab tests comparing cmb Budweiser to strong Budweiser are repeated = strong beer is stronger than cereal malt beverage.
- Even with the differing units of measurement – alcohol by weight vs. alcohol by volume – strong beer is stronger than cereal malt beverage.
- Economic analysis of simply moving the strong beer products to 2300 additional outlets shows a loss of 217 retail liquor stores.
- Do not expect to save Kansas jobs and businesses by preserving spirits on their shelves. Any type of retailer can tell you that sales depend on traffic. Customer traffic will be reduced if their highest volume products are sold elsewhere.

State Regulatory Licensing –

There are a wide variety of state policies relating to how liquor is sold, and they reveal both the priorities of that state and the history of how prohibition was repealed in that particular state. Kansas has a particular issue relating to its constitution which makes changes to the definition of cereal malt beverage potentially unconstitutional as it changes the definition of alcoholic liquors / intoxicating liquors – a reference included in our constitution. **Kansas represents an excellent balance between the desires of those who would expand access and availability and those who would prefer a more regulated model.**

- **There are 17-18 control states.**
- **Of those, 6 states have city owned retail liquor stores and rarely allow private providers. 10 states have only state owned retailers, which allow no one but the state to sell spirits and/or wine. This may be paired with the sale of beer through licensed outlets.**
- **Many states differentiate the sale by packaged stores and convenience stores or grocery stores and the products they may carry, whether it is allowing wine in grocery stores, or 3.2 cereal malt beverages only.**
- **6 have separate licensing for 3.2 cereal malt beverage. In fact, some actually differentiate whether or not the product sold may be refrigerated. It is not correct to paint Kansas as the most strictly regulated of these states. In my research, one analysis painted New York as having very lenient liquor laws – and yet, New York does not allow wine or liquor sales in grocery stores.**
- **In fact, the majority of states do not have unrestricted licensing systems regarding allowing strong beer, wine and spirits to be sold by grocery and convenience stores and none have the system proposed in this bill.**
- **It is not true that states are rushing to open up their laws. The most recent major structural changes to licensing structures happened in the eighties. South Dakota has been used as an example. That state, much like Missouri, allowed grocery stores to get into the liquor business around 1986.**
- **Proposals for Strong Beer and Wine sales have been rejected in recent years in Massachusetts, New York, Tennessee, Oklahoma and Colorado. Oklahoma and Colorado have very similar systems to our own. Deregulation also failed in Oregon.**
- **New Mexico has a system that allows for the transfer/sale of licenses because it has only 1000 licenses for the sale of spirits, wine and beer (on AND off premise). There are no other types of off premise licenses available. That restriction hasn't changed for 25 to 30 years and the result is that it can cost $300,000 to $700,000 to buy one of these licenses. Recently, NM created a restaurant license for selling wine and beer.**
- **Many states have distance or population restrictions for the number of liquor licenses issued. Kansas only has the restriction of prohibiting a liquor license within 200 feet of a church, school or college.**

The Case for Compliance

- **Kansas retail liquor stores have proven compliance rates in preventing underage sales – typically ranging from 80% to as high as 88%. There are <u>no statewide compliance rates</u> for grocery and convenience stores.**

- Now, the proponents would have you believe that they are better than liquor stores at checking I.D.s. They use tobacco compliance numbers to make this case. National statistics show that convenience and grocery stores have a worse record than liquor stores as it relates to selling alcoholic beverages.

- Tobacco sales = inventory separate from other items for sale / 18 year olds selling to 18 year olds

- The Kansas ABC does not track underage alcohol-sale compliance in convenience and grocery stores. It only tracks underage alcohol-sale compliance for Kansas owned retail liquor stores. Anyone who makes this claim is comparing convenience and grocery store tobacco compliance rates to Kansas liquor store alcohol compliance rates. This is comparing apples to oranges.

- What is a fact is that convenience and grocery stores have a much higher failure rate nationally than liquor stores when it comes to selling alcohol to minors. The National Research Council Institute of Medicine found 70% of minors nationwide purchase their alcohol from grocery and convenience stores.

- It also took the state of Kansas hundreds of thousands of dollars in order to get convenience stores to reach a high compliance rate! In 2005, Kansas convenience stores had a tobacco sales compliance rate of 62%.

- At that time, this forced Kansas to choose between taking a $5.4 million reduction in SRS block grant funds or pay a $2.2 million penalty to be used to raise the compliance rate. Is Kansas prepared to make the same investment again to develop compliance rates for the new category of licensees? See costs attached.

Please oppose deregulation of the Kansas retail liquor system.

This is not what is best for Kansas.