



## SUMMARY OF INITIATIVE 1105

Concerning liquor (beer, wine, and spirits).

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### BRIEF SUMMARY

Initiative 1105 (I-1105) amends state laws regarding the distribution and sale of spirits in Washington. Washington is a control state, meaning the state has exclusive control over the distribution of spirits and the retail sale of spirits in the original package. I-1105 eliminates the state's exclusivity and privatizes the distribution and sale of spirits (hard liquor).

### BACKGROUND

The Washington State Liquor Control Board (LCB) regulates the manufacture, distribution, and sale of liquor (spirits, beer, and wine) in the state. Any entity seeking to participate in any capacity in the manufacture, distribution, or sale of liquor must obtain the appropriate license to do so from the LCB, and is then limited to participating in the manner authorized by the license. The extent of the regulation varies based on the type of liquor and licensed issued.

#### Sale and Distribution of Beer and Wine

Washington has what is known as a three-tiered system, meaning an entity can either manufacture, distribute, or sell beer and wine. Historically, an entity was prohibited from operating in more than one tier, though a number of licenses grant the holder the ability to participate in multiple tiers. For instance, licensed wineries and breweries are authorized to manufacture, distribute, and sell their own products. The separation of tiers was enforced through the "tied-house" law, which prevented an entity from having a direct or indirect financial interest in an entity that operates in a different tier. Washington's tied-house prohibition was repealed by the Legislature in 2009 and direct and indirect financial interests between and among industry members and retailers are now permitted so long as the financial interest does not result in undue influence or have an adverse impact on public health and safety.

"Undue influence" means the ability of one retailer or industry member to directly or indirectly influence the purchasing, marketing, or sales decisions of another retailer or industry member by any agreement or other business practice. "Adverse impact on public health and safety" means a result that is more likely than not to result in alcohol being made significantly more attractive or

available to minors, or is more likely to result in overconsumption, consumption by minors, or other harmful or abusive forms of consumption.

Beer and wine manufacturers, distributors, and retailers are also subject to a number of pricing controls. Manufacturers and distributors must maintain a price list showing the prices at which beer and wine will be sold (price posting), and are prohibited from selling at a price differing from the price shown on the list (uniform pricing). Quantity discounts are prohibited, and manufacturers and distributors cannot sell at a price below acquisition/production cost.

### Sale and Distribution of Spirits

Regarding distilled spirits, Washington is a control state, meaning the LCB is the only entity that can distribute spirits and sell spirits in original packaging. Licensed distilleries are authorized to sell their spirits at retail; however, the distilleries are required to buy any spirits they sell at retail (or sample) from the LCB. Restaurants and bars authorized to sell spirits must also buy their spirits from the LCB.

There are 161 state liquor stores and 155 contract liquor stores throughout the state, and one state-run distribution center that supplies all the state and contract liquor stores as well as the restaurants and bars licensed to sell spirits.

The state currently levies and collects a liter tax and a sales tax on spirits and the rate varies depending on whether the spirits are purchased by a consumer or a restaurant licensee. Revenue from the sales taxes is deposited in the state general fund and distributed to local governments.

The state also collects a mark-up on spirits sales. Mark-up refers to the difference between the price the LCB pays for a bottle of spirits and the price for which the LCB sells it. The mark-up is deposited into the liquor revolving fund and is used to fund LCB activities. Excess funds in the liquor revolving fund are distributed to the state general fund and to local governments.

State law directs the LCB to set aside in a separate account a certain amount of its gross sales of liquor to restaurant and similar licensees for deposit in the state general fund and distribution to local governments.

The LCB enters into agreements with tribes for tribes to operate tribal liquor stores. Tribes purchase liquor from the LCB at a negotiated price and pay sales and liter taxes on those purchases except that taxes are not paid on a quota based on tribal membership.

The state entered into agreements with tribes regarding fuel taxes in which the tribes charge their customers a fuel tax equivalent to the state motor vehicle fuel tax. The tribes receive 75 percent of the tax revenue collected and the state receives 25 percent.

## **SUMMARY OF INITIATIVE 1105**

### The Liquor Control Board

The LCB must stop operating all state liquor stores, and sell all inventory and assets of state liquor stores and the distribution center by April 1, 2012.

If necessary, the LCB may report to the Legislature on the need for legislation which may include provisions for the retraining of state workers displaced by the privatization of spirits retail or distribution.

### Spirits Retailer

The initiative creates a spirits retailer license, allowing the license holder to sell spirits for off-premise consumption. The LCB must notify all qualifying spirits retailer license applicants no later than July 1, 2011, that they are licensed to sell spirits at retail. Persons holding a spirits retailer license may start selling spirits on November 1, 2011.

The LCB must develop criteria for the issuance of spirits retailer licenses. In considering applicants for a spirits license, emphasis should be placed on: inventory management systems; employee training; employee supervision, and physical security of the spirits. The LCB is encouraged to make spirits retailer licenses available to existing contract liquor stores.

Spirits retailer licensees must pay the LCB 6 percent of their gross annual spirits sales. This amount applies for a five-year period beginning on the date the licensee first sells spirits and is deposited into the state general fund. Each retail spirit licensee must also pay an annual license fee determined by the LCB. The LCB must establish rules for reporting the volume of sales and the frequency and timing of the payments of the 6 percent of a licensee's gross annual sales.

A retail spirit licensee may only purchase spirits from a licensed spirit distributor.

### Spirits Distributor

The initiative creates a spirit distributors license that allows the sale of spirits to any person licensed to sell spirits, to other distributors, and for export. The LCB must notify all qualifying spirits distributor applicants no later than July 1, 2011, that they may distribute spirits. All persons who are authorized by a spirits manufacturer, supplier, or distiller, to distribute products in the state are eligible for a spirits distributor license unless the LCB determines issuance of a license is not in the public interest. Persons holding a spirits distributor license may start selling spirits on October 1, 2011.

Spirits distributor licensees must pay the LCB 1 percent of their gross annual spirits sales which is deposited into the state general fund. This amount applies for a five-year period beginning on the date the licensee first sells spirits. Each spirits distributor must also pay an annual license fee determined by the LCB. The LCB must establish rules requiring spirits distributor licensees to report the volume of sales and the frequency and timing of the payments of the 1 percent of a licensee's gross annual sales.

The "distributor appointment" required to be filed with the LCB by manufacturers and other suppliers must identify each distributor authorized to distribute its products and all brands that each distributor may distribute. This requirement applies to the distribution of spirits, beer, and wine.

The pricing and delivery laws currently applicable to beer and wine manufacturers and distributors are applicable to spirits manufacturers and distributors. However, distributors may offer quantity discounts of spirits.

### Taxes and Mark-up

The initiative repeals the existing mark-up, liter tax, and sales tax on spirits sales. The existing state and local retail sales tax would apply to spirits sales.

By January 1, 2011, the LCB must report to the Legislature on a recommended rate of taxation to be paid by spirits distributors within the state. The tax is to be calculated on a per-liter basis of all spirits sold to distributors within the state. The rate of taxation paid by spirits distributors must generate the same annual revenue for state and local jurisdictions as the current tax system, as well as at least an additional \$100 million dollars in projected revenue minus expenses over a five-year period beginning November 1, 2011.

In determining the rate of taxation, the LCB must consider other spirits-related revenue including business and occupation taxes, increased taxable spirits inventory base, and license fees.

### Tied-House Law

A spirits manufacturer, distiller or retailer licensee may not possess any direct or indirect interest in a spirits distributor license or liquor importer's license or in an entity that possesses a spirits distributor license or liquor importer's license.

### Other

The LCB must promulgate a rule regarding the sale of spirits to tribes on terms consistent with and no less favorable to tribes than the current rules. At the request of any federally recognized tribe, the LCB may negotiate an agreement to replace any current liquor tax compact with an agreement to share amounts equal to liquor taxes collected on sales within the reservation at percentages comparable to fuel tax compacts.

By January 1, 2011, the LCB is directed to prepare a report to the Legislature recommending the method by which to carry out the intent of the initiative pertaining to the rights of tribes or military installations within the state of Washington to sell or purchase spirits.

The Office of the Code Reviser must prepare legislation for the 2011 session removing all statutory reference to the term "state liquor store." The effective date of the legislation must be April 1, 2012.

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