

# Control State Politics

## Big Alcohol's Attempt to Dismantle Regulation State by State

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### Executive Summary

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With Big Alcohol seeking to increase profit margins, across the U.S. powerful corporations and misguided politicians are promoting plans to eliminate state control of alcohol sales, promising better prices and selection in return for less alcohol regulation. As states become more desperate for revenue, a booming alcohol business could overshadow the protection of public health and economic stability.

Currently the biggest threats are efforts to privatize alcohol sales, in which control states would sell their liquor stores and distribution centers and license private businesses to sell alcohol. Selling the state's assets and collecting license fees would generate a one-time cash windfall, an argument that proponents use to grow support for privatization in the present economic climate. Absent from their promises, however, are acknowledgements of the longer-term losses of annual income that states will experience and the significant threat of privatization to the public's health and safety. Research shows that privatization will result in substantial harm to the public's health and safety. States will experience higher economic costs stemming from increased outlet density, increased consumption, and increased alcohol-related injuries and violence.

### *Major Findings*

- State control of alcohol sales benefits the public's health. Control state residents consume less spirits and less alcohol in general than in license states. Also, control states collect more than three times as much revenue per gallon of alcohol sold as spirits.
- Transferring control from the state to private businesses will lead to increased outlet density, alcohol consumption, and alcohol-related harm while depriving the state of millions of dollars in annual revenue.
- Privatization is linked with dramatic increases in outlet density and resulting levels of alcohol-related harm. For example, higher outlet density is strongly associated with suicide, assault, and other violence.
- Control states have significantly lower rates of youth drinking and binge drinking, as well as lower rates of alcohol-impaired driving deaths, than license states.
- Studies of British Columbia and Alberta, Canada, the United Kingdom, Sweden, Iowa, and West Virginia have shown that privatization leads to increased consumption and harm, and decreased revenue.



- Economic estimates predict that with privatization in either Virginia or Washington State, spirits sales would rise by 21 percent and total alcohol consumption would increase as much as 7 percent.
- Increased consumption in either Virginia or Washington State will cause an estimated \$50 million per year in harm paid from state coffers (mostly criminal justice costs), and \$1 billion per year in total harm costs.
- Privatization in either state will decrease annual state alcohol revenue by \$200-\$300 million.
- If Virginia privatizes its retail monopoly on spirits, researchers estimate 220 more alcohol-related deaths would occur each year.
- Under Virginia Governor Bob McDonnell's proposal, the number of stores selling spirits would more than triple from 322 to 1,000.
- Privatization in Washington State would drastically increase the number of retail outlets from 316 to as many as 3,357 private licensed outlets, approximately the same number of total McDonald's and Starbucks locations in the state.
- Costco has been fighting Washington State's alcohol regulations for years, first in court, then in the legislature; now the company is taking its cause to the voters.
- Costco is the number one contributor to Initiative 1 100 in Washington State, donating \$807,000 in cash and \$377,879 in in-kind contributions to date.
- Wal-Mart has contributed another \$40,000 to support I-1 100 in Washington State.
- The sole financial supporters of Initiative 1 105 in Washington State, Young's Market and Odom-Southern, have contributed a total of \$2,244,000 to date.
- The beer industry has become a major supporter of the campaign to defeat both privatization initiatives in Washington State, donating close to \$5 million to date.
- The Virginia governor's office has met numerous times with Big Alcohol players such as Diageo, MillerCoors, and the Distilled Spirits Council of the United States, the lobbying arm of the spirits industry.
- From 2008-2010, Virginia Governor Bob McDonnell received \$448,407 from Big Alcohol including Anheuser-Busch InBev, Diageo, and Associated Distributors.

### *Recommendations*

- Politicians should stop using alcohol regulation as a bully pulpit for calling for smaller government; alcohol is regulated because it is potentially harmful.
- A history lesson for all governors, state legislators, and their staff is in order to understand the horrible conditions that led to Prohibition, and why 18 states chose to control the sale of alcohol to protect public health and safety.
- State regulatory agencies need to play a more vocal role in protecting the public's interests. Many alcohol regulators also need a history lesson so they understand why their jobs are so important and why they should speak out to defend control and regulation in general.



- The two national alcohol trade groups representing state regulators (the National Alcohol Beverage Control Association and the National Conference of State Liquor Administrators) each need to distance themselves from industry influence and politics and do more to stop the erosion of state-based alcohol control and regulation.
- Each branch of the federal government should help strengthen the role of states in the regulation of alcohol and not undermine state authority. Passage of H.R. 5034 (CARE Act) would be a good first step.
- A single-issue focus for public health groups (e.g., drunk driving) is no longer sufficient; advocacy organizations need to recognize the critical importance of state regulation.
- Alcohol control allies must work in concert to alert state residents to the harm and cost to their states from privatization, and urge them to oppose any privatization voter initiatives, legislation, or court challenges to control systems.
- Better scrutiny is needed over the political influence of the alcohol industry and its retail arm, the big box chain stores who are behind current privatization efforts.
- Voters should not believe the rhetoric of Big Alcohol that deregulation is better for consumers and call upon their legislative leaders to protect the public over profit.
- Washington State voters should vote "No" on both privatization initiatives there.
- Instead of considering the privatization of alcohol sales, states should ensure future economic and public health benefits by not only maintaining but strengthening their control of alcohol sales.



# Control State Politics

## Big Alcohol's Attempt to Dismantle Regulation State by State

### Introduction

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With Big Alcohol seeking to increase profit margins, across the U.S. powerful corporations and misguided politicians are promoting plans to eliminate state control of alcohol sales, promising better prices and selection in return for less alcohol regulation. As states become more desperate for revenue, a booming alcohol business could overshadow the protection of public health policy and economic stability.

Privatization rhetoric deploys two general themes: the philosophical and the fiscal. Proponents of privatization argue that the government should have limited power and that a free market would efficiently regulate alcohol, as with any other commodity.

Politicians and businesses eager to expand their markets echo this sentiment, failing to acknowledge that even license systems do not enjoy a completely free market. Proponents and companies also attempt to make an economic case, promoting the financial allure they see privatization offering both the state and business.

The battle over the control of alcohol sales and distribution may seem like any other rhetorical debate over the role of private industry and government regulation. But there is an important difference: the demonstrated likelihood of privatization to increase the number of lives lost, damaged, and forever changed by alcohol over-consumption.

This report was prompted by the current debate raging in two key states: Washington and Virginia. While there has been much news coverage of both battleground states, what has been missing is a proper historical context and policy understanding of the origins of control states in the first place. Empty rhetorical references to “outdated laws” or “big government” purposefully ignore the unique and necessary regulatory history of alcohol. The goal of this report is to explain the importance of maintaining what's left of the control state system and not let profit motive and politics trump public health and safety.

What often gets left out of the news and political rhetoric, and what this report covers, include: the substantive scientific literature that supports the state control of alcohol to protect the public; the political players and industry infighting in the privatization battles; and two current examples to serve as case studies of the threat to state control: Washington State and Virginia.

### Brief History of State Control of Alcohol

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When Prohibition ended, the Twenty-First Amendment gave states the authority to create new regulatory and enforcement systems for the sale and consumption of alcoholic beverages. After the pervasive lawlessness of the Prohibition era, states wanted to restore legitimacy to the government and law enforcement while minimizing alcohol consumption and its various associated harms – the conditions that led to Prohibition in the first place. The idea was to balance people's desire for legal alcohol sales with the government's interest in protecting public health and safety.



Two models were proposed for state regulation. Under the control model, states are directly involved with alcohol sales; under the license model, state agencies issue licenses to private businesses to sell alcohol subject to the state's regulation and enforcement. Both systems aim to create and preserve a three-tiered structure—producer, distributor, and retailer—intended to keep any one company from seizing too much control of the market, thereby avoiding vertical integration.

Ultimately, 18 states and four counties (all in Maryland) adopted control models. The other 32 states implemented license systems. The control models vary to some extent among states based on which products are controlled and which tiers are run by the state, but all express a policy of restricting alcohol availability to reduce consumption and associated problems.<sup>1</sup> The 18 original control states are still considered control states, though several have eroded the extent of control over the last 76 years, by either privatizing the wholesale or retail tier or by privatizing the sale of one or more types of alcoholic beverage. The table below details the current composition.

## Control Jurisdictions<sup>2</sup>

<i>State</i>	<i>Spirits</i>	<i>Wine</i>
Montgomery Co., MD	Wholesale/Retail	Wholesale/Retail
New Hampshire	Wholesale/Retail	Wholesale/Retail
Pennsylvania	Wholesale/Retail	Wholesale/Retail
Utah	Wholesale/Retail	Wholesale/Retail
Alabama	Wholesale/Retail	License
Idaho	Wholesale/Retail	License
Maine	Wholesale/Retail	License
North Carolina	Wholesale/Retail	License
Ohio	Wholesale/Retail	License
Oregon	Wholesale/Retail	License
Vermont	Wholesale/Retail	License
Virginia	Wholesale/Retail	License
Washington	Wholesale/Retail	License
Mississippi	Wholesale	Wholesale
Wyoming	Wholesale	Wholesale
Iowa	Wholesale	License
Michigan	Wholesale	License
Montana	Wholesale	License
West Virginia	Wholesale	License

## Many Benefits of State Control of Alcohol

Many peer-reviewed research studies published in scientific journals demonstrate that state alcohol control benefits the public's health. Yet privatization proponents claim that privatization does not pose any threat to public health and safety. They refuse to acknowledge the published findings from studies



showing the harm privatization causes to the public.<sup>3</sup> They also cite reports from private organizations whose missions are to promote limited government and fewer business regulations, rather than to promote safety and reduce harm to the public.<sup>4,5</sup>

So here are the facts. Residents of control states consume 14 percent less spirits and 7 percent less alcohol than in license states, while government sees more than three times as much revenue per gallon of alcohol sold as spirits.<sup>6</sup> Consumption is lower in control states due to less alcohol availability; there are fewer spirits stores, shorter operating hours, more restrictions on advertising and packaging, and control of excessive discounting.<sup>7</sup> State retail store employees are also likely to have better training and experience to prevent underage or inebriated drinkers from purchasing alcohol.<sup>8</sup>

In addition, control states have lower outlet density. That is, the number of locations where alcoholic beverages are available for purchase, either per area or population.<sup>9</sup> Higher outlet density is correlated with alcohol-related harm. Studies show strong associations between alcohol outlet density and suicide, assault, and other violence.<sup>10,11</sup>

In contrast, privatization is linked to dramatic increases in outlet density. In states where wine was privatized, wine sales and consumption increased significantly.<sup>12</sup> Studies also found a 9.5 percent increase in spirits consumption and a net increase in total alcohol consumption after Iowa privatized spirits. Contrary to common privatization rhetoric regarding border states, no changes were found in spirits sales in states bordering Iowa.<sup>13</sup>

Control states have significantly lower rates of youth drinking and binge drinking, as well as lower rates of alcohol-impaired drinking deaths. In control states, fewer high school students reported drinking alcohol in the past 30 days (14.5 percent), and fewer reported binge drinking in the past 30 days (16.7 percent), as compared to license states. Lower consumption rates were associated with a 9.3 percent lower alcohol-impaired driving death rate under age 21 in control states.<sup>14</sup>

The harmful consequences and costs of privatization are not limited to the United States. Researchers have found these large-scale effects in other countries as well, especially Canada. For example, privatization of liquor outlets in British Columbia has contributed to increased alcohol sales and alcohol-related harm.<sup>15</sup> In Alberta, which completely privatized its system, prices and consumption increased while the province took in \$500 million less than it did under its control system. Moreover, the public welfare in Alberta was reduced, along with tax revenue.<sup>16</sup>

Since the United Kingdom significantly deregulated its system, alcohol has become so cheap and available in stores that traditional pubs are going out of business. More troubling, underage drinking rates are twice as high as they are in the United States, and the incidence of alcohol-related disease and death has increased, especially among women and youth.<sup>17</sup>

A recent study of Sweden predicted incredible growth in alcohol-related harm if privatization systems were adopted there: alcohol consumption would increase between 17 and 37 percent, with estimates of 770 to 2,000 more deaths, 8,500 to 20,000 more assaults, and 2,700 to 6,600 more drinking-driving offenses per year.<sup>18</sup>

The benefits of state alcohol control are clear: lower consumption, especially by underage youth; less alcohol-related harm; and a stable source of revenue for state services and programs. But good public policy and common sense rarely stops industry from lobbying to further its own interests over that of the public.



## Big Alcohol Push for Deregulation

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The alcohol industry, with its ever-increasing power, perpetuates the erosion of state control. While budget cuts decrease states' ability to enforce existing alcohol laws, mammoth corporations that make up Big Alcohol grow bigger through vertical and horizontal integration, disintegrating the once-distinct separation of tiers.

The biggest alcohol producers diversify by purchasing smaller companies to add new brands of beer, wine, and spirits to their product portfolio. They also purchase and consolidate distributors wherever they can, to cut costs and again, own more of the market. These conglomerates use their growing power to influence the political process, contributing to campaigns for privatization (and other deregulation) efforts, political candidates, and elected officials in state, local, and federal elections. They argue that price and tax increases target the poor, that regulations penalize responsible drinkers, and that restrictions on the industry will lead to job losses.<sup>19</sup>

While the current privatization battles are taking place at the ballot box (in Washington) and in the legislature (in Virginia), industry has previously attempted to use the court system to strip states of its regulatory power. For years, Costco (the main proponent of privatization in Washington) has been waging battle through litigation as well.

One such legal challenge went as far as the Supreme Court of the United States. In *Granholm v. Heald*, the Court struck down laws in Michigan and New York that permitted direct shipping from in-state wineries but forbade it from out-of-state.<sup>20</sup>

*Granholm* should have been a narrow decision about discrimination between in-state and out-of-state wineries, but there has since been a proliferation of lawsuits to expand *Granholm's* meaning to allow further deregulation.<sup>21</sup> Various lawsuits have challenged volume caps, online retailers and license restrictions, supplier-owned wholesaler operations, and in-person purchase requirements.

Also hoping the court system would be its ticket to deregulation, Costco sued the Washington State Liquor Control Board in 2004, claiming that its restrictions on beer and wine sales violated federal anti-trust laws. Arguing they were anti-competitive, Costco challenged nine important regulations:

1. **Uniform pricing:** breweries and wineries must sell a particular product at the same price to every distributor. Distributors must sell the beer and wine products to every retailer at the same price they have posted.
2. **Price posting:** beer and wine distributors shall file with the board a price posting showing the wholesale prices at which any and all brands of beer and wine sold by such distributor shall be sold to retailers within the state.
3. **Post and hold:** beer and wine manufacturers must hold their posted prices for at least 30 days.
4. **Minimum markup:** distributors and suppliers must price their products at no less than 10 percent above their acquisition costs.
5. **Ban on volume discounts.**
6. **Ban on sales of beer and wine on credit.**



7. *Delivered price requirement*: distributors must sell beer and wine at the same delivered price to all retailers even if the retailer pays the freight and picks up the goods itself.

8. *Central warehousing ban*: retailers prohibited from storing or taking delivery of beer and wine at a central warehouse.

9. *Prohibition on retailers selling beer and wine to other retailers.*<sup>22</sup>

The Ninth Circuit Court of Appeals ultimately upheld all of the state's restrictions except the post and hold requirement. Costco has also experienced disappointment on the legislative front. As recently as February 2010, state legislators sponsored three privatization bills for consideration. Not one of them has passed to date.<sup>23</sup> Having failed in the courts and legislature, industry has now turned to the voters.

## **Battleground: Washington**

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In Washington and Virginia, the interests of a few major players threaten to privatize the states' control policies at the expense of public health and reliable state revenue. Huge retail and distribution operations drive these plans as part of their industry's constant push for deregulation. The interests and political power of big business are clear in Washington State, where major retailers and distributors are campaigning to dismantle the state's regulatory system.

Currently, the state controls the sale of spirits through the Liquor Control Board. In fiscal year 2009, the system generated \$333 million in taxes and net income.<sup>24</sup> Sixty percent (\$199 million) went to the state's general fund, 19 percent (\$63 million) funded services provided by cities and counties, and the remaining 8 percent (\$71 million) supported health and prevention programs and research.<sup>25</sup>

More than two-thirds (\$222 million) of the alcohol-related revenues came from taxes on spirits. Now, two statewide initiatives on the ballot threaten to eliminate both the steady source of income and the states' regulatory power to protect the public from alcohol-related harm.

Initiative 1100 (I-1100), filed by the "Modernize Washington" campaign, would close the state liquor stores, replace them with privately owned outlets, and allow for in-state distillers and importers to sell directly to retailers. But I-1100 does not stop there. I-1100 would also remove current state law that requires uniform pricing and price posting, and bans volume discounts, credit, warehousing, and retailer-to-retail sales.

Eliminating these controls would benefit big box retailers like Costco Wholesale Corporation and Wal-Mart, whose business models are based on volume discounts. Issaquah, Washington-based Costco does \$70 billion in annual sales with 550 locations around the world.<sup>26</sup> Trying to deregulate Washington's control system in one fell swoop, Costco is I-1100's number one contributor, donating \$807,000 in cash and \$377,879 in in-kind contributions to date, and even having its employees gather petition signatures in Costco stores. Wal-Mart has contributed another \$40,000 to support I-1100 as well. In total, the supporters of I-1100 have contributed more than \$2 million to date.<sup>27</sup>

Playing on widespread public concern about the economy, Costco claims that privatization would benefit the public, offering drinkers greater selection at a lower price while making alcohol sales more efficient than under the current system. I-1100 would not only privatize spirits, but also deregulate all types of beverage alcohol, including beer and wine. Big box retailers could directly negotiate volume



discounts and favorable terms with huge, multi-national suppliers, shutting out smaller retailers and suppliers such as local, independent breweries and wineries from the market.

Moreover, I-1100 allows producers, importers, and distributors to maintain interests in retail locations, meaning the distribution tier can be bypassed completely or integrated into another tier. Costco already partners with Big Alcohol to make vodka and tequila products that are branded with the Kirkland Signature line, and sells them in its license-state stores. Restaurant chains that are members of Costco buy large amounts of supplies there, including alcohol. Expansion of the Kirkland Signature brand of alcohol is a major driver of Costco's support of I-1100.<sup>28</sup>

Complicating the deregulation fray, Initiative 1105 (I-1105) also calls for the state to close its stores and instead license private parties as spirits retailers or distributors. Unlike I-1100 however, I-1105 maintains the three-tier system, requiring a distribution tier (private not public) between the supplier and retail levels.

I-1105 also maintains the state's price control mechanisms, although it would allow volume discounts for spirits. I-1105 would require licensees to pay the state a percentage of their gross spirits sales; repeal certain taxes on retail spirits sales; and direct the Liquor Control Board to recommend a tax to be paid by spirits distributors,<sup>29</sup> although there is no certainty that the tax legislation would be passed.

Although the committee sponsoring I-1105 is the Washington Citizens for Liquor Reform, the initiative is entirely funded by two distributors: Young's Market and Odom-Southern. These big distributors oppose I-1100, which would put them out of business, or at least end their distribution power. Young's Market Company is a \$2.05 billion business, based in Southern California with operations in eight states.<sup>30</sup> Odom-Southern is a distribution partnership formed between Odom Corporation, based in the Pacific Northwest, and Southern Wine and Spirits.<sup>31</sup> Southern Wine and Spirits is the largest wine and spirits distributor in the United States, the 38th largest business in the United States, and had \$8.4 billion in revenue in 2009.<sup>32</sup> Young's and Odom-Southern have contributed a total of \$2,244,000 to the effort to date.<sup>33</sup>

Though I-1105 calls for less deregulation than I-1100, both initiatives evoke strong opposition from the public health and social service fields. A statewide coalition of health care, churches, teachers, treatment and prevention, and union workers have formed an opposition group called Protect Our Communities to oppose both initiatives.<sup>34</sup>

Governor Christine Gregoire also opposes the measures, and warned, "At the worst time in our history, we would be losing a sizeable amount of revenue."<sup>35</sup> Gregoire also cautioned against increasing problems with impaired driving and domestic violence.

Even some players within the alcohol industry oppose the measures. Without current state regulation, craft brewers and small wineries will have to fight for shelf space at retail outlets.<sup>36</sup> The Washington Wine Institute acknowledged, "Some of those legal protections have probably helped the Washington wine industry get where it is today, by providing a level playing field for access to retailers."<sup>37</sup>

Recently, the beer industry has made major contributions to the "No" campaign. The National Beer Wholesalers Association and the Beer Institute (representing the nation's beer manufacturers) have donated \$2 million each, while the Washington Beer and Wine Wholesalers Association has contributed \$975,000 to the campaign to defeat both initiatives. In total, the "No" campaign has received roughly \$5.8 million in cash donations and an additional \$175,000 in in-kind donations to date.<sup>38</sup>



The Washington State Auditor's Office issued a report in early 2010 listing four possible options for partial or full privatization of liquor sales, including: 1) privatizing the state distribution center in Seattle; 2) privatizing retail sales and increasing the number of stores; 3) privatizing the retail sector and allowing for market factors to determine the number of retail outlets; and 4) completely privatizing liquor distribution and sales, and taxing spirits at a flat rate.

The report estimates that privatization could generate \$277 million in revenue over five years while drastically increasing the number of retail outlets from 316 state and contracted stores to as many as 3,357 private licensed outlets,<sup>39</sup> approximately the same number of total McDonald's and Starbucks locations in the state.<sup>40</sup>

The Auditor's report also found that completely removing the state from liquor sales and placing a flat tax on liquor—the option that I-1100 espouses—would have the most significant impact on consumption. Based on comparisons with privatized state systems, spirits consumption in Washington could increase as much as 15 percent in future years.<sup>41</sup>

I-1100 would essentially open the door for Costco and other big box corporations to serve as all three tiers of the alcohol system: producer, wholesaler, and retailer. Costco and other retailers such as Wal-Mart and Safeway would walk hand in hand with Diageo and other Big Alcohol corporations to own alcohol sales in Washington State—a model Costco will use for the few other control states left, especially those with ballot initiative processes. In other states, the governor and legislature are the targets.

## **Battleground: Virginia**

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In Virginia, attempts to privatize the state alcohol control system date back at least forty years and have been almost constant since the 1980s. The last five governors have either suggested privatization or indicated they would sign into law a bill from the legislature, but nothing ever came to fruition. Now the rhetoric has become more heated.

While running for governor in 2009, Governor Bob McDonnell pledged to privatize the system and use the funds to improve the state's transportation network. He said he hasn't met anyone who thinks selling Jack Daniels whiskey or Grey Goose vodka is a core function of government.<sup>42</sup> This year he put privatization plans on a fast track.

After months of special interest and town hall meetings, the governor's office unveiled his proposal in early September. McDonnell's privatization plan predicts a one-time windfall of \$458 million that would be deposited in a new "infrastructure bank" to fund grants and loans for transportation projects. The singular influx of cash would be a combination of \$33 million from selling off liquor store properties; \$160 million from wholesale license fees; and \$265 million (minimum) from auctioning retail licenses. The proposal also includes \$229 million in annual revenue from license renewals and taxes for core services such as education, with some money earmarked for substance abuse prevention and 22 new Alcoholic Beverage Control enforcement officers.

Under McDonnell's proposal, the number of stores selling spirits would more than triple from 322 to 1,000. Licenses would be auctioned to the highest bidders from 600 big-box and grocery stores; 250 convenience and drug stores; and 150 package stores. Annual license renewal would cost between



\$500 and \$2,000, depending on store size. A company would be limited to holding 25 percent of the licenses in any one tier.

Although McDonnell presented the plan as a way to find money for transportation without raising taxes, three types of new taxes are included in the proposal: a 2.5 percent tax on restaurants and bars that choose to buy spirits directly from wholesalers instead of retailers; a \$17.50/gallon excise tax charged at the wholesaler level; and a one percent tax on gross receipts charged to wholesalers.<sup>43</sup>

Despite the Republican governor's optimistic forecasts, Democratic leaders oppose the plan, saying it won't yield nearly as much as McDonnell promises and will cut off a steady source of income in the process.<sup>44</sup> Some Republican legislators are not convinced either. Delegate Brenda L. Pogge (R-York) opposes the plan, saying that it will be a hard sell to the public: "There's three things that are called taxes in the plan, but they're going to say it doesn't raise taxes?"<sup>45</sup>

Del. Lacey E. Putney (I-Bedford), head of the powerful House Appropriations Committee and a McDonnell ally, has indicated that he thinks the current alcohol control system in Virginia works well. Putney, an Independent who sits in the House Republican majority, is the latest member of the GOP caucus to express doubts about McDonnell's plan. Putney described the amount of revenue McDonnell promises to direct to transportation from his privatization plan as "pocket change."<sup>46</sup>

The same day that McDonnell's privatization plan was unveiled, the Washington Post ran an editorial posing serious questions about the plan's long-term viability. While the Virginia Department of Alcoholic Beverage Control currently nets \$324 million annually from alcohol taxes and profits, McDonnell's plan is vague about whether the proposed alcohol taxes will completely replace the amount of annual revenue lost, and whether the new tax income would grow over time, as the current system's revenue is projected to do. In addition, the one-time \$458 million windfall is not enough to match the annual transportation needs in Virginia—it would not come close to the amount needed to maintain current Virginia roads for even six months.<sup>47</sup>

McDonnell's opponents point out that privatization would eliminate thousands of state jobs, with no guarantee those employees would be hired by new private stores.<sup>48</sup> Loss of those state jobs would also add up in pension payouts, costing the state millions more in the process.

Local law enforcement officials also worry that they will not be given adequate zoning authority, and will end up with a liquor store on every corner and less ability to protect public safety in their communities. The Virginia Association of Chiefs of Police acknowledged that private liquor interests want to increase consumption, but hope that an increase in consumption doesn't equal an increase in alcohol-related violations. An attorney representing retailers recently inexplicably denied there would be any increase in outlets: "It's not like it's going to be 800 new buildings selling liquor."<sup>49</sup> Yet privatization will mean 1000 locations selling liquor that were not doing so before.

A 1993 study by Price Waterhouse demonstrated that if the Virginia alcohol control system were privatized, the price of liquor would have to increase in order for the privatized system to be revenue-neutral. The state would also have to add as many as 46 more regulatory agents to handle increased tasks of licensing, regulation, and enforcement of alcohol sales. The ABC accounting department would also need to add another 16 staff positions to ensure adequate collection of state taxes that are currently included in the state's price markup. Robert Colvin, a previous ABC commissioner, expressed a significant concern that the resources would not be adequate to properly address the increased workload in a privatized system.<sup>50</sup> So much for smaller government.



Also, and most significantly, somehow the governor is choosing to ignore estimates that if Virginia privatizes its system, 220 more alcohol-related deaths would occur each year.<sup>51</sup> Moreover, estimates point to spirits sales rising by 21 percent and total alcohol consumption increasing by as much as 7 percent. Increased consumption will cause an estimated \$50 million per year in harm paid from state coffers (mostly criminal justice costs), and \$1 billion per year in total harm costs. Privatization is also likely to decrease annual state alcohol revenue by \$200-\$300 million.<sup>52</sup>

Various corporations and trade groups with an interest in the sale of alcohol are influencing the governor's inner circle. For example, Costco and Wal-Mart, along with Kroger, Safeway, and Food Lion, are among the major retail chains that formed an alliance called the "ABC Privatization Coalition" to support deregulation efforts.<sup>53</sup>

In addition, five lobbyists from the lobbying firm Eckert Seamans are working on the campaign. Since July 2010, Eckert Seamans has made three \$10,000 political contributions to the Republicans' Virginia House Campaign Committee, the Democrats' Commonwealth Victory Fund, and the governor's Opportunity Virginia political action committee.<sup>54</sup>

Large alcoholic beverage producers also have an interest in bolstering their bottom lines through deregulation. Though suppliers and trade organizations officially profess neutrality on privatization, the governor's office has met numerous times with powerful industry players such as Diageo, MillerCoors, and the Distilled Spirits Council of the United States (DISCUS), the lobbying arm of the spirits industry.<sup>55</sup> Big Alcohol is a constant presence in Virginia state politics, spending thousands of dollars lobbying the state General Assembly.<sup>56</sup> During 2008-2010, McDonnell received \$448,407 from alcohol producers and wholesalers including Anheuser-Busch InBev, Diageo, and Associated Distributors.<sup>57</sup>

Meanwhile, smaller retailers from the Virginia Retail Federation and the Virginia Petroleum, Convenience, and Grocery Association have expressed their concern to Governor McDonnell and urged him to request the assembly's investigative arm to conduct a study of the financial assumptions behind his proposal. These groups worry that spirits licenses would fall mostly to the biggest retail corporations—the ones pushing for privatization at the same time that they contribute large amounts to the governor's campaign.<sup>58</sup> Also, recently a religious coalition has formed to oppose privatization.<sup>59</sup>

McDonnell's staff proposes a quick transition to a private system. They say licenses could be auctioned in a year and new stores could start to stock their shelves in September 2011.<sup>60</sup> A vote on the proposal from McDonnell's own 31-member government reform commission is scheduled for the first week of October. Then McDonnell will call a special session of the General Assembly to consider the privatization question in November.

## Industry Infighting over Alcohol Control

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The privatization fight is not only about the alcohol industry and state governments; it reflects opposing interests within the alcohol industry as well. While the fight in Washington between distributors and big box retailers presents an obvious division over industry interests, other players prefer to play behind the scenes. Still, large producers such as Anheuser-Busch InBev and Diageo benefit from a privatized



system where they dominate the competition. Also, producer trade groups even lobby for special privileges like direct shipping so they can “compete” with smaller suppliers.

Spirits producers want to normalize their product as much as possible, making it available at the same number of locations as beer and wine. Small producers (breweries, wineries, and distilleries) worry that privatization will eliminate the level playing field that state control provides and allow big retailers and suppliers to negotiate deals that edge the smaller brands off the shelves.

While suppliers and their trade organizations such as the Distilled Spirits Council of the United States say that they are neutral on the privatization issue, they support privatization efforts in various ways. DISCUS representatives recently attended several stakeholder meetings in Virginia, one at which they gave a presentation saying that there is no public health impact of privatization in control states.<sup>61</sup>

And, recently David Ozgo, chief economist for DISCUS, wrote a guest column in the Oregonian newspaper arguing that control states are no better than license states in preventing alcohol problems. Listing unreferenced, anonymous “government” data regarding alcohol consumption, highway fatalities, and underage drinking, Ozgo argued that some control states, including Oregon, have rates above the national average (without naming or discussing that average).<sup>62</sup>

Also, since the Granholm Supreme Court decision, numerous lawsuits have been filed to challenge various state laws that pit one industry group against another. In an effort to curtail such litigation, United States Representative Bill Delahunt (D-Massachusetts) has introduced House Resolution 5034, which would protect the state’s authority to regulate alcoholic beverages.<sup>63</sup> The Act reinforces that under the Twenty-First Amendment, the state is the best venue to address alcohol policy. While the bill is strongly supported by beer, wine, and spirits wholesalers (because it supports state laws that require separation of the tiers), a number of industry groups such as the Wine Institute have come out in strong opposition.<sup>64</sup>

It’s just this sort of industry infighting over state regulation that contributes to a lack of awareness and understanding of the public health and safety benefits of strong laws. As long as the public and policymakers think it’s all just an industry food fight, the science and historical context to support strong state regulation gets lost in the shuffle.

## **Public Health Groups Must Fight for State Regulation**

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The data is clear. Estimates associated with privatization in either Virginia or Washington point to spirits sales rising by 21 percent and total alcohol consumption increasing as much as 7 percent. Increased consumption, in either state, will cause an estimated \$50 million per year in harm paid from state coffers (mostly criminal justice costs), and \$1 billion per year in total harm costs. Privatization will also decrease annual state alcohol revenue by \$200-300 million.<sup>65</sup>

Alexander Wagenaar, an epidemiologist at the University of Florida and author of multiple studies on the effects of privatization on public health said it best: “If you make it easier to drink, people drink more. And if people drink more, we have more alcohol-related problems. It’s as simple and basic as that.”<sup>66</sup> Unfortunately, while there is strong research to support state control of alcohol, there is not strong enough advocacy coming from the public health sector. Too often groups do not recognize the erosion of alcohol regulation until it is too late, if at all.



Ultimately, privatization is a fight about who gets to sell and profit from the sale of alcohol. Despite the abundance of evidence describing how state control of alcohol sales improves the health and well-being of residents and provides considerable, stable income to states, Big Alcohol continues to lead the charge to eliminate those benefits.

Public health advocates need to recognize that the current fights are not limited to just Washington State or Virginia, or even to just the control states. The decisions to maintain or eliminate alcohol control in Washington and Virginia will have far-reaching effects. In the few remaining control states, from Idaho to Pennsylvania, the idea of privatizing alcohol sales is a perennial consideration, especially during economic downturns. Politicians seeking office suggest privatization as a way to fulfill campaign promises as other sources of revenue shrink. Big Alcohol and big box retailers will no doubt enjoy greater sales and consumption of their products if deregulation spreads throughout the 18 remaining control states. Moreover, the march for deregulation is a constant in the license states as well. California has become the poster child for the erosion of regulation over the years, as alcohol is sold almost everywhere there, and is certainly not a model to be followed.

Transferring control from the state to private business will lead to increased outlet density, alcohol consumption, and alcohol-related harm while depriving the state of millions of dollars in annual revenue. Instead of considering the privatization of alcohol sales, states should ensure future economic and public health benefits by maintaining their control of alcohol distribution and retail.

Coalitions of public health and alcohol control allies must work in concert to alert state residents to the harm and cost to their states from privatization, and urge them to vote down any privatization voter initiatives, and tell their lawmakers to do the same. The time has come for groups whose missions have been too narrowly focused on issues such as “drunk driving” or “underage drinking” to take a strong stand in support of state control. While some groups may think that how alcohol products are sold is not relevant to their mission, indeed it is at the very core of preventing alcohol harm.

## Recommendations

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- Politicians should stop using alcohol regulation as a bully pulpit for calling for smaller government; alcohol is regulated because it is potentially harmful.
- A history lesson for all governors, state legislators, and their staff is in order to understand the horrible conditions that led to Prohibition, and why 18 states chose to control the sale of alcohol to protect public health and safety.
- State regulatory agencies need to play a more vocal role in protecting the public's interests. Many alcohol regulators also need a history lesson so they understand why their jobs are so important and why they should speak out to defend control.
- The two national alcohol trade groups representing state regulators (the National Alcohol Beverage Control Association and the National Conference of State Liquor Administrators) each need to distance themselves from industry influence and politics and do more to stop the erosion of state-based alcohol control and regulation.



- Each branch of the federal government should help strengthen the role of states in the regulation of alcohol and not undermine state authority. Passage of H.R. 5034 (CARE Act) would be a good first step.
- A single-issue focus for public health groups (e.g., drunk driving) is no longer sufficient. Advocacy organizations need to recognize the critical importance of state regulation.
- Alcohol control allies must work in concert to alert state residents to the harm and cost to their states from privatization, and urge them to oppose any privatization voter initiatives, legislation, or court challenges to control systems.
- Better scrutiny is needed over the political influence of the alcohol industry and its retail arm, the big box chain stores who are behind current privatization efforts.
- Voters should not believe the rhetoric of Big Alcohol that deregulation is better for consumers and call upon their legislative leaders to protect the public over profit.
- Washington State voters should vote “No” on both privatization initiatives there.
- Instead of considering the privatization of alcohol sales, states should ensure future economic and public health benefits by not only maintaining but strengthening their control of alcohol sales.

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*This report was prepared by Sarah Mart and Michele Simon, with assistance from Megan DeLain.*



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