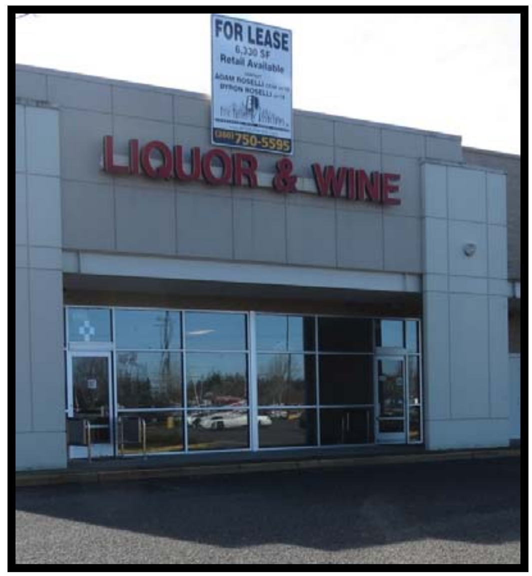
Campaign for a Healthy Alcohol Marketplace

JULY 2014 NEWSLETTER

Washington Privatization:
Promises made, promises broken



Despite the many promises made by proponents of Washington State's privatization Initiative 1183, the citizens of that state didn't reap major benefits.

In the Initiative ad campaign, proponents claimed the benefits of privatization would include lower prices, no new taxes, more convenience, more money for public safety, better enforcement, and a free market economy for alcohol where many businesses could flourish. These were major selling points for "getting the government out of the liquor business." But aside from being able to get major brands of hard liquor at more locations, the rest of these promises have fallen flat:

- Prices are higher not lower.
- Large new taxes, called "fees," pushed prices up.
- Law enforcement got <u>no</u> additional money. Instead, law enforcement must contend with a major new problem of liquor theft involving youth and organized criminals.
- Revenue collections are high thanks to sale of assets, special one-time fees, high prices and additional outlets. However, this level cannot be sustained after one-time fees sunset and sales are complete.
- Instead of a "free market" economy with opportunities for entrepreneurs of all sizes, Washington got a market heavily dominated by large national corporations. The wholesale spirits market went from state ownership to a near duopoly with two national companies immediately gaining 93% market share. The retail market quickly became dominated by large national grocery chains thanks to all the advantages written into the measure by the Initiative's sponsors. Almost one-third of the small liquor stores have closed or never opened. Many of the rest may not survive. Small distilleries and wineries lost the state liquor stores as a sales outlet and have difficulty getting on the shelves of large grocery chains. Restaurants aren't getting the lower prices they anticipated.
- Convenience has little impact on the general public because the vast majority does not shop regularly for hard liquor. A survey conducted by the state of Washington in 2010, revealed that only

46% had shopped in a liquor store during the entire year. Of those 46%, only 10% shopped weekly.

- Although it is too early to assess social impacts, the Initiative was not constructed in a way that would limit adverse consequences.
- This Initiative illustrates what can happen when a true public process is not used to write laws for the public.

The November 2011 Initiative Measure that changed 60 pages of Washington alcohol law was sponsored by and financed almost entirely by the Costco Corporation. (Costco contributed 99.5% of the total campaign donations. The next highest donors were Safeway and Trader Joe's which contributed $50,000 each. All other donations were under $400.)

Why would Costco spend over $20 million dollars on a ballot measure especially after spending millions trying to change regulations via lawsuits and lobbying? It is likely that Costco wanted to use its vertically integrated business model to sell spirits and, particularly, wine. (Costco, the 19th largest company in the US with over $100 billion in sales, is the largest retailer of wine in the US.) Costco pioneered the idea of merging retail and wholesale functions and selling products at deep discounts in a large warehouse-style store. However, such vertical integration was not legal for alcohol sales due federal and state law.

The US three-tiered regulatory model features a strong wholesale tier which acts as a buffer between the manufacturer and retailer. In most states, this tier also collects the excise tax and tracks products to ensure safety. When the three tiers are not separate entities, the "orderly market" can break down, leading to price wars and aggressive sales practices that appeal to problem drinkers and price-sensitive youth. Tax loss and tainted alcohol products can become problems as they do in other countries.

Costco first tried to change Washington state law through lawsuits and legislative action. While this effort garnered small changes, they turned to the initiative process for large-scale, fundamental change. Their first attempt, in 2010, failed. But they returned in 2011, with greater funding and a revised measure that included deregulation of wine and privatization of spirits, but left beer regulations alone. They were hoping to eliminate the beer industry's opposition. This measure passed and was implemented seven months later.

A better public process would have allowed input from all stakeholders including public health and safety as well as small business. Research could have been used to structure the measure to minimize social impacts. Strategies could have been developed to ensure a fair and level marketplace where large and small businesses could be profitable. Unfortunately, that did not occur and Washington will need several more years to iron out problems with this Initiative.

The new report will be available for download at www.healthyalcoholmarket.com by August 1.

For more information, see www.healthyalcoholmarket.com
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