

Treasury Board Submission – Request for Decision

Minister: Honourable Shirley Bond, Solicitor General

Ministry: Public Safety and Solicitor General

Date: 18/01/2012 Ministry Document #: 24-12

Title: Options for the Distribution of Liquor

Issue:

This submission explores options of changing the business model for distribution of liquor, and its potential impact on the financial plan of the province.

Request:

This submission is seeking Treasury Board direction on which option(s) government wishes to pursue, and permission to issue a public RFI or RFP to obtain the financial information required to assess the cost/benefit of the option(s).

Background / Context:

The distribution of liquor in the province is a mixture of public and private services. (Note: the reference to distribution is the process of getting liquor to the stores, bars and restaurants that sell to consumers, not the retail system itself). The main elements of liquor distribution in the province are:

- The LDB operates two warehouses in Vancouver and Kamloops that distribute approximately 55 per cent of the liquor sold in the province by value including: all spirit products, all imported wine, a portion of BC wine (mostly to government stores) and some beer.
- LDB warehouses distribute to government liquor stores (GLS), most large private liquor stores and a portion of bars/restaurants
- Breweries and beer agents distribute most beer to GLS, private stores and larger bars/restaurants.
- BC wineries distribute most of their products purchased by wholesale customers.
- GLSs sell products to many medium to lower volume bars/restaurants.
- The LDB requires the agents of imported products to store the products in private agent stocking program (ASP) warehouses upon entry to the province - LDB warehouses receive their supply of these products from ASP warehouses. The company ContainerWorld is the largest ASP warehouse. Most imported beer is represented by the large breweries (Molson, Labatt, Sleeman) who act as their own ASP warehouse and integrate these products with the distribution of their domestic products.

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Contact: Lori Wanamaker
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Honourable Shirley Bond

Date Signed



Cabinet Concept Paper

Ministry: Public Safety and Solicitor General

Date: 01/12/2011

Issue: Liquor Retail and Distribution Model Options

Description:

The current BC liquor distribution model is a mixed public-private retail/wholesale model. There have been several reviews over the past decade, resulting in incremental increases in private sector retailing.

A wholesale private company has recently brought forward a proposal to take over the warehousing and distribution operations.

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Background/Context

The current mixed model includes approximately 1400 retail locations to purchase liquor (including licensee retail stores, rural agency stores, private wine stores, on-site manufacturer stores, and duty-free stores); 197 of which are government liquor stores (GLSs) selling beverage alcohol to retail and wholesale customers. Although GLSs account for only 15% of total retail liquor stores in the province, they account for almost 50% of liquor sales to retail customers.

Store Type	Number of Stores
Government Liquor Stores	197
Licensee Retail Stores	672
Rural Agency Stores	221
Other (wine stores, manufacturer stores, duty free stores)	307

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The wholesale beverage alcohol distribution model includes two government distribution centres, GLSs and a number of manufacturers and private distributors that are authorized to distribute beverage alcohol as agents of the LDB. Beverage alcohol is purchased by LDB from over 400 suppliers and manufacturers, including licensed manufacturers within BC (wineries, distilleries and breweries).

There will be human resource issues to consider with any model option other than status quo. It is anticipated that the BCGEU would take a strong position against any change in the model and there could be loss of higher paying jobs. The human resource impacts and their magnitude will vary depending on the delivery model (for example, ASD or complete or bundled sale of stores) and the timing. For example, the current Collective Agreement expires March 2012.

Liquor Retail and Distribution Options:

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Contact: Lori Wanamaker, Deputy Solicitor
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December 5, 2011

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Value in the B.C. Liquor Distribution Model

Premise:

This is an update of the 2006 proof of concept regarding option for the retail and wholesale distribution of liquor in BC. It updates the summary analysis provided in 2006 to reflect the 2010-2011 service planning and financial reporting periods. The discussion is primarily from a financial perspective and explicitly excludes the flat tax proposal raised in 2006.

Background:

The BC model has been reviewed several times over the last 10 years:

2002	CORE review of LDB
2003	Introduction of LRS licenses
2005	Review of retail/wholesale/tax model
2006	2006 ASD Wholesale Proposal
2007	Signing of GEU agreement
2011	Exel Wholesale ASD proposal

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Of note, the 2007 decision to leave 197 government retail liquor stores open has left the province with a mixed retail model, where GLS are competing with LRS, with different rules of operation governing each. This decision was taken in order to gain union support of the BCGEU in the 2007 negotiations.

Opportunity:

The value of a license to sell retail liquor has significant value due to the moratorium on the issuance of any additional licenses. As well, the current mixed model of liquor distribution and retailing in BC is capital intensive and there is the potential to free up some or all of this capital through the sale or outsourcing of the remaining public sector parts of the operations.

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Retail Operations:

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- The facilities are a mix of owned properties and leased properties, with various amounts of leasehold improvements embedded.

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Wholesale/Warehousing/Distribution Operations:

- The wholesale beverage alcohol distribution model in BC includes the two government distribution centres, brewers distributors ltd., 7 bonded warehouses and a number of manufacturers and private distributors that are authorized to distribute beverage alcohol as agents of the LDB.

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- Specifically, Exel has brought forward a proposal to take over the warehousing and distribution operations, and has put an attention grabbing value of \$100 million in "inventory and land assets".

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Appendix A: Extracts from the BCLDB Service Plan

BUSINESS OF THE LIQUOR DISTRIBUTION BRANCH

The LDB operates a province-wide, retail/wholesale beverage alcohol business, within a mixed public-private model. As of December 31, 2010, the LDB:

- has a workforce of approximately 3,500 full- and
- part-time employees;
- operates 197 GLSs throughout the province;
- operates two distribution centres, in Vancouver
- and Kamloops; and
- has a Head Office facility in Vancouver.

The LDB purchases beverage alcohol from more than 400 suppliers and manufacturers within the province, across the country and around the world. Licensed manufacturers in BC include 222 wineries, 57 breweries, and 16 distilleries.

With more than 1,300 beverage alcohol retail outlets operating in BC, consumers have a variety of choices depending on their service needs, including:

- 197 GLSs (government-owned and –operated stores selling beverage alcohol to retail and wholesale customers);
- 672 licensee retail stores (LRSs – private stores licensed to sell all beverage alcohol products);
- 223 rural agency stores (RASs – general merchandise stores in rural communities authorized to sell all beverage alcohol products);
- 251 on-site manufacturer stores (stores at wineries, breweries and distilleries that sell the products that they manufacture);
- 34 off-site manufacturer stores (stores operated by the BC wine industry that sell BC winery products);
- 12 private wine stores; and
- 11 duty-free stores.

The wholesale beverage alcohol distribution model in BC includes the two government distribution centres, GLSs and a number of manufacturers and private distributors that are authorized to distribute beverage alcohol as agents of the LDB.

PERCENTAGE OF GROSS \$ SALES BY SALES CHANNEL 2009/10

Government Liquor Stores	40.7%
Licensee Retail Stores	33.5%
Licensees (pubs, bars, restaurants)	17.6%
Agency Stores	8.2%

Excerpts from the BCLD Service Plan Report:

"In 2010/11, the Liquor Distribution Branch's (LDB) sales were \$2.82 billion which was 1.2 per cent less than the previous year. Sales increases were in the spirits and wine categories but this was offset by significant decreases in the beer and refreshment beverage categories. Net income for the year was \$890.4 million which was \$13.1 million more than the previous year but significantly short of the budgeted \$973.7 million. We are confident that consumer confidence will improve and that we will once again be achieving our sales and net income objectives."

"In 2010/11, the number of retirements at the LDB continued to increase. In an effort to ensure a smooth transition and minimize operational impacts, we continued to focus on our succession planning."

Appendix B: BC LDB Financial Statements

BRITISH COLUMBIA LIQUOR DISTRIBUTION BRANCH

BALANCE SHEET

(in \$000s)

As at March 31,	2011	2010
		(note 17)
ASSETS		
CURRENT ASSETS		
Cash	-	6,724
Accounts receivable	5,013	5,307
Inventories (note 3)	83,021	89,974
Prepaid expenses (note 4)	4,979	4,294
Due from Province of British Columbia	9,229	-
	<u>102,242</u>	<u>106,299</u>
LONG TERM ASSETS		
Prepaid expenses - long term (note 4)	3,377	2,090
Intangible Assets (note 5)	2,884	2,785
Property, plant and equipment (note 6)	57,626	59,397
	<u>166,129</u>	<u>170,571</u>
LIABILITIES		
CURRENT LIABILITIES		
Bank indebtedness	7,153	-
Accounts payable and accrued liabilities	141,177	137,447
Current portion of deferred tenant allowances (note 7)	85	85
Current portion of tenant improvement loans (note 8)	158	361
Current portion of obligation under capital lease (note 9)	47	74
Due to Province of British Columbia (note 10)	-	13,773
	<u>148,620</u>	<u>151,740</u>
LONG TERM LIABILITIES		
Deferred tenant allowances (note 7)	348	432
Tenant improvement loans (note 8)	61	219
Obligation under capital lease (note 9)	129	176
Other long term liabilities (note 14)	16,971	18,004
	<u>166,129</u>	<u>170,571</u>

Commitments and contingent items (notes 11 & 12)

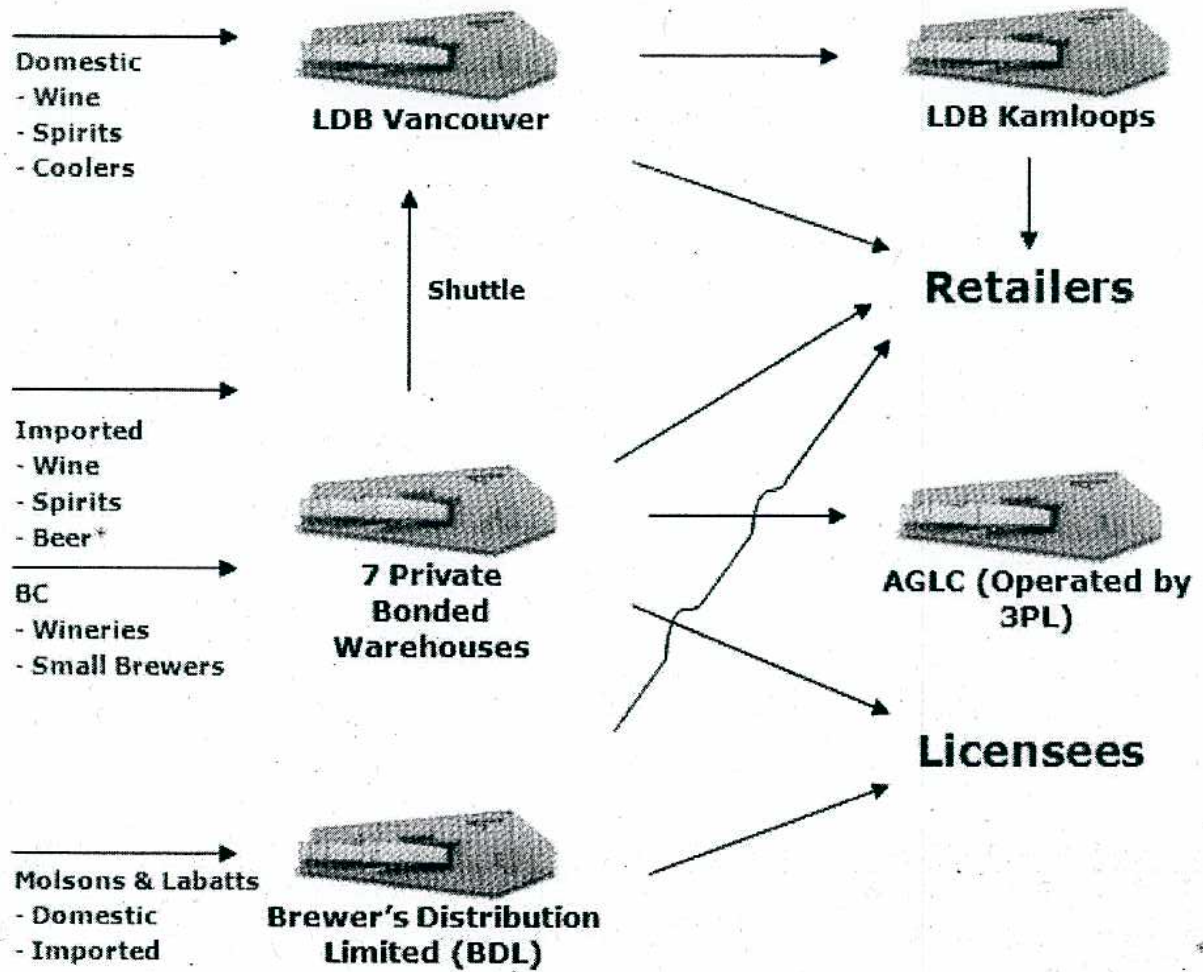
Approved by:


Jay Chambers
General Manager



Roger M. Bissoondatt, CA, CMA
Chief Financial Officer

Appendix C: Liquor Distribution Model in BC today:



Appendix D: Tax model definitions

ALCOHOL PRODUCTS TAXATION: INTERNATIONAL
EXPERIENCES
AND SELECTED PRACTICES IN ASIA

By
Somchai Richupan, Ph.D.
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III. INTERNATIONAL EXPERIENCES OF TAXATION ON ALCOHOL.

3.1 Tax Rates.

Alcohol tax rates can be classified into 4 types, Specific, Unitary, Ad Valorem and Combination.

1. Specific

Taxes applied on a specific basis are expressed in terms of a uniform rate (or fixed amount) based on the volume of alcohol content usually as X units of currency per liter of pure alcohol or as X unit of currencies per liter per degree of alcohol content. This is particularly appropriate since it is alcohol contained in the product which is the common denominator between spirit drinks of different types and origins. For example, the United States, applies excise tax on all spirits at the rate of US\$ 13.50 per US proof gallon of pure alcohol. Chinese Taipei applies excise tax on reprocessed alcohol beverages that alcohol content less than 20% by volume at NT\$, 7 per liter per degree of alcohol content.

2. Unitary

Taxes applied on a unitary basis are expressed in terms of a fixed amount for a given quantity of product, irrespective of strength, usually as 'y' units of currency per liter. For example, Singapore levies excise tax on beer (stout and porter) at the rate of \$3.70 per liter.

3. Ad Valorem

Ad valorem taxes are expressed as a percentage of the value of the product. Thus, the higher the value of the product, the greater the amount of tax which is payable.

4. Combination rate

Combination rates are a combination of the specific/unitary and ad valorem methods of applying taxes. They generally consist of a specific rate and an ad valorem rate. For example, the excise tax levied by Thailand on beer is either 55% ad valorem or 100 baht per liter of pure alcohol whichever is higher.

3.2 The Tax Base.

The tax base is the amount on which the tax rate is applied. The tax base can be either the physical quantity or the monetary value of the product.

Physical Quantity Bases

In the case of alcohol products physical quantity is generally measured in terms of the physical volume of the liquid in liter or in gallon. The quantity being measured could be either the quantity of the product which normally is in the form of liquid containing some degree of alcohol or the quantity of the alcohol content in the product depending on whether the unitary or the specific rate is applied.

Monetary Value Bases.

The monetary value of the product is often referred to the selling price. However, the selling price can be either price inclusive of tax or price exclusive of tax. In most developed countries, it is customary to quote and charge prices exclusive of indirect taxes and the purchasers pay the price plus the taxes explicitly. However, in most developing countries such customs does not exist. In most developing countries, selling prices are usually quoted inclusive of tax so that when the purchaser pays the selling price he has already paid the tax implicitly. Taxes are not visible because they have

already been buried in the prices. This gives rise to the distinction between the inclusive rate and exclusive rate. Inclusive rate refers to the tax rate which is applied on the selling price inclusive of tax. The exclusive rate refers to the tax rate which is applied on the selling price exclusive of tax.