HB 598

Department of Legislative Services

Maryland General Assembly
2016 Session

FISCAL AND POLICY NOTE
First Reader

House Bill 598 (Delegate Frick)
Economic Matters and Ways and Means

Alcoholic Beverages - Distribution and Sales Tax Revenues

This bill requires the Comptroller to remit to each county any alcoholic beverage sales tax revenues collected that is greater than the amount collected for fiscal 2017, beginning in fiscal 2018. Furthermore, the bill authorizes the Montgomery County Department of Liquor Control (DLC) to (1) authorize the wholesale distribution of beer to a person who purchases DLC's interest as a franchisee and (2) sell its interest in any dispensary to a Class A beer and wine license holder or any person who meets the requirements to obtain such a license. In either case, the sale must be done through a public auction.

The bill takes effect July 1, 2016, contingent on the enactment of Senate Bill 724 of 2016.

Fiscal Summary

State Effect: General fund revenues decrease by $10.2 million in FY 2018 and by $41.9 million in FY 2021 due to the bill's redistribution of alcoholic beverage sales tax revenue to local governments. Expenditures are not affected.

($ in millions)	FY 2017	FY 2018	FY 2019	FY 2020	FY 2021
GF Revenue	$0	($10.2)	($20.4)	($32.3)	($41.9)
Expenditure	0	0	0	0	0
Net Effect	$0.0	($10.2)	($20.4)	($32.3)	($41.9)

Note:() = decrease; GF = general funds; FF = federal funds; SF = special funds; - = indeterminate effect

Local Effect: Local government revenues increase by $10.2 million in FY 2018, $20.4 million in FY 2019, $32.3 million in FY 2020, and $41.9 million in FY 2021. Montgomery County revenues and expenditures generally decrease, resulting in a net negative impact, to the extent that DLC sells its interests as authorized by the bill; however, the exact impact of the bill on Montgomery County finances cannot be reliably estimated, as discussed below.

Small Business Effect: Potential meaningful. A small business may benefit if it purchases part of DLC's interests to expand its own business.

Analysis

Bill Summary: The additional alcoholic beverage sales tax revenue must be remitted back to the counties based on the proportion of alcoholic beverage sales tax revenue that was collected from each county.

The sale of DLC's interest in wholesale beer to a franchisee removes DLC's monopoly on the wholesale distribution of beer that is distributed under the franchise. The Montgomery County Board of License Commissioners must issue a person a Class A beer, wine, and liquor license within 60 days if that person purchases DLC's interest in a dispensary. DLC may not sell its interest in more than 25 dispensaries and may not sell more than one to any person.

Current Law: The general sales and use tax is imposed on a bracket basis approximating 6%. Chapters 571 and 572 of 2011 increased the sales tax rate on the sale of an alcoholic beverage from 6% to 9%. The general 6% tax rate applies to charges for labor, materials, or property used in connection with the sale of an alcoholic beverage and to a mandatory gratuity or service charge in the nature of a tip for serving food or any type of beverage to a group containing more than 10 individuals. The alcoholic beverage sales tax accrues to the general fund.

In Montgomery County, the liquor control board is authorized to sell any kind of alcoholic beverage and the county may sell alcoholic beverages through the use of a county liquor dispensary. Furthermore, in Montgomery County, no person, firm, or corporation may keep for sale any alcoholic beverage not purchased from DLC. Unless otherwise specified by law, no retailer may sell or deliver any alcoholic beverage in Montgomery County for resale except to a county liquor dispensary. Holders of a Class 6 limited wine wholesaler's license or a nonresident winery permit may sell or deliver wine directly to a restaurant, county liquor dispensary, or other retail dealer in Montgomery County, and the holder of a direct wine shipper's permit may ship wine directly to consumers in Montgomery County.

Background: In general, most Maryland jurisdictions permit the sale of alcoholic beverages through a three-tier system in which retail alcoholic beverages licensees (first tier) purchase alcoholic beverages from licensed Maryland wholesalers (second tier) who purchase alcoholic beverages from licensed manufacturers and import companies (third tier). In Montgomery County, DLC operates a dispensary system that acts as the second-tier wholesaler for retail alcoholic beverages licensees in the county. Furthermore, there is only one Class A beer, wine, and liquor license issued in Montgomery County;

people who want to purchase liquor for off-premises consumption must generally buy from a county-operated liquor store.

Montgomery County issued revenue bonds in 2009, 2011, and 2013 that are backed by a pledge of annual revenue derived from DLC. The county has about $114 million in outstanding debt backed by this source, which requires debt service of about $10 million annually. Montgomery County advises that the bill likely results in a breach of the county's contract with its bondholders, and that this may lead to (1) the trustee declaring the bonds to be in default due to the changes in pledged revenues; (2) a forced downgrade of the outstanding bonds as well as the bond rating agency putting the bonds on negative outlook; and/or (3) refinancing of the bonds to general obligation bonds.

As shown in **Exhibit 1**, in fiscal 2014, Montgomery County DLC expenditures totaled $239.2 million, while revenues totaled $268.7 million; $26.4 million (approximately 10% of total revenues) was transferred to the Montgomery County general fund. The debt service payment on DLC revenue-backed bonds was $9.8 million in that same year. Additionally, DLC had about 400 employees in fiscal 2014.

Exhibit 1
DLC Sales and Transfers to the Montgomery County General Fund
Fiscal 2010-2014
($ in Millions)

	FY 2010	FY 2011	FY 2012	FY 2013	FY 2014
Total Expenditures	**$204.7**	**$215.4**	**$220.2**	**$225.7**	**$239.2**
Debt Service Payments	3.8	3.7	6.4	6.4	9.8
Total Revenues	**$229.3**	**$242.8**	**$252.3**	**$259.3**	**$268.7**
Total Retail Sales	106.2	113.7	120.0	122.4	127.2
Total Warehouse Sales	121.2	127.1	130.4	134.4	139.4
Total Sales	**227.4**	**240.8**	**250.4**	**256.8**	**266.6**
License and Other Revenue	1.9	2.0	1.9	2.5	2.1
General Fund Transfers	**$29.0**	**$26.2**	**$28.5**	**$25.7**	**$26.4**

Source: *Montgomery County Department of Liquor Control Annual Report*, fiscal 2014; *Montgomery County Comprehensive Annual Financial Report*, fiscal 2014

State Revenues: The bill sets the total revenue collected in fiscal 2017 from the alcoholic beverage sales tax as the maximum amount that may be deposited into the general fund from that tax and requires the Comptroller to remit any additional revenues back to the local governments. Therefore, as shown in **Exhibit 2,** general fund revenues decrease by $10.2 million in fiscal 2018 and by $41.9 million in fiscal 2021. This estimate is based off of the fiscal 2017 alcoholic beverage sales tax revenue estimate, which is $288.9 million and projected to increase by approximately 3.5% annually.

Exhibit 2
Projected Alcoholic Beverage Sales Taxes and Impact of the Bill
Fiscal 2017-2021
($ in Millions)

	FY 2017	FY 2018	FY 2019	FY 2020	FY 2021
GF Revenues – Current Law	$288.9	$299.0	$309.2	$321.1	$330.8
GF Revenues – Under the Bill	288.9	288.9	288.9	288.9	288.9
GF Revenue Loss (to Locals)	**$0.0**	**-$10.2**	**-$20.4**	**-$32.3**	**-$41.9**

Note: Totals may not sum due to rounding.
Source: Comptroller's Office, Department of Legislative Services

Local Revenues: Due to the bill's changes to the distribution of the alcoholic beverage sales tax, Baltimore City and county revenues increase by $10.2 million in fiscal 2018, $20.4 million in fiscal 2019, $32.3 million in fiscal 2020, and $41.9 million in fiscal 2021.

Local Fiscal Effect: To the extent that DLC sells its interests as is authorized by the bill, Montgomery County revenues decrease as DLC receives less revenue from its wholesale and dispensary operations. Expenditures decrease correspondingly as DLC scales back its own operations due to savings on staff, purchasing of alcoholic beverages, and other industry-related operating costs. Revenues increase significantly from any ongoing franchise fees and other revenues collected by DLC through the sale of its interests; however, this revenue is not expected to fully offset DLC's revenue loss. For example, Montgomery County advises that the net profit generated by 25 dispensaries is about $19.2 million per year. To fully offset the revenue loss in just the first year, each dispensary would need to sell for $792,000 at the public auction.

Furthermore, revenues that would normally be transferred to the Montgomery County general fund from DLC may be affected. Over the preceding five fiscal years, DLC has transferred an average of $27 million annually to the Montgomery County general fund. It is likely that some or all of this revenue is lost as DLC sells off its interests. County general fund expenditures may also increase by as much as $10 million annually as Montgomery

County is forced to pay the debt service on bonds that were originally issued and backed by revenues derived from DLC and alcoholic beverage sales.

The net impact of the bill on Montgomery County finances depends on numerous factors including the decision of DLC to sell off its interests, when it chooses to do so, and the outcome of any resulting public auctions, and thus, cannot be reliably estimated.

Additional Information

Prior Introductions: None.

Cross File: None.

Information Source(s): Montgomery County, Comptroller's Office, Department of Legislative Services

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md/hlb

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