

ANALYSIS

Item 93: Oregon Liquor and Cannabis Commission Liquor Sales and Card Fees

Analyst: Michelle Deister

Request: Increase Other Funds expenditure limitation for the Oregon Liquor and Cannabis Commission by \$2,562,734 for administrative expenses related to bank card fees, by \$11,881,048 for store agent compensation payments, and by \$3,733,000 for Distillery Agent Compensation payments, due to liquor sales in excess of legislatively adopted budget forecasts.

Analysis: The Oregon Liquor and Cannabis Commission reports that liquor sales for the 2021-23 biennium are exceeding forecasts upon which Other Funds expenditure limitation for agent compensation and bank card fee payments was predicated. The legislatively adopted budget assumed gross liquor sales of \$1.6 billion, and per bottle surcharge revenues (which are retained by the General Fund) of \$41.3 million. Based on sales data, the OLCC is now assuming gross sales of \$1.68 billion, and surcharge revenue of \$39 million. The increase in sales and assumed revenue is being driven mostly by inflation and by consumer choice of higher end products, rather than by volume. Because bank card fees and compensation payments to store and distillery agents are figured as a percentage of sales revenue, the agency requires additional expenditure limitation to pay the amounts due to its partners under contract.

Per ORS 471.810, liquor revenue remaining after agency expenses -- which include operations, fees, and agent compensation payments and cost of goods -- is distributed to the General Fund (56%), cities (20%), City Revenue Sharing (14%), and counties (10%). The increase in sales is expected to result in an additional \$22.2 million in liquor revenue available for distribution per statute, as follows:

	<u>LAB with February 2022 Adjustments</u>	<u>September 2022 Sales Projections</u>	<u>Difference</u>
General Fund (includes surcharge revenue)	\$ 346,187,269	\$ 357,571,449	\$ 11,384,179
Incorporated Cities	\$ 108,876,924	\$ 113,813,842	\$ 4,936,918
City Revenue Sharing	\$ 76,213,847	\$ 79,669,689	\$ 3,455,842
Counties	\$ 54,438,462	\$ 56,906,921	\$ 2,468,459
Mental Health (privilege tax receipts)	\$ 20,296,910	\$ 20,296,910	-
Oregon Wine Board (privilege tax receipts)	\$ 745,142	\$ 745,142	-
Distribution Total	\$ 606,758,554	\$ 629,003,953	\$ 22,245,398

Recommendation: The Legislative Fiscal Office recommends that the Emergency Board increase Other Funds expenditure limitation for the Oregon Liquor and Cannabis Commission by \$2,562,734 for administrative expenses related to bank card fees, by \$11,881,048 for store agent compensation payments, and by \$3,733,000 for Distillery Agent Compensation payments, due to liquor sales in excess of legislatively adopted budget forecasts.

Request: Increase Other Funds expenditure limitation by \$18,176,782 to accommodate payments for bank card fees and liquor agents, as a result of increased liquor sale revenue projections.

Recommendation: Approve the request.

Discussion: The request for the \$18.2 million increase in Other Funds expenditure limitation is comprised of three components: bank card fees, liquor store agent compensation, and distillery agent compensation.

Bank Card Fees

The request for additional Other Funds expenditure limitation for bankcard fees is related to the increase in sales of liquor in-stores by people using credit cards. The Oregon Liquor and Cannabis Commission (OLCC) pays bankcard fees related to all sales of liquor. The agency determines the need for bankcard fees by multiplying the percentage of sales estimated to be paid by consumers with bank cards/credit cards. The bank card costs have increased significantly above the forecasted legislatively approved budget levels for the current biennium and are expected to exceed the current approved budget limitation. Total liquor sales in the 2021-23 biennium are five percent above the forecast. In addition, liquor sales to consumers, who may use credit cards to purchase liquor, are eight percent above forecast. The percentage of bank card usage for liquor purchases increased from 80 percent to 90 percent in April 2022. The 90 percent usage rate of bank cards has continued in the current biennium. The legislatively approved budget forecast for bank card expenditures assumed an 80 percent usage rate, which was the rate before the pandemic for liquor purchases. Additional costs associated with Elavon, the state Treasury approved bank cards service provider, has increased. The 2021-23 Legislatively Approved Budget (LAB) provides \$17.9 million in limitation for bank card fees. Based on the updated forecast, OLCC anticipates the new amount needed for bank card fees is \$20.5 million. The difference results in a \$2.6 million Other Funds expenditure limitation increase for bank card fees for the remainder of the biennium.

Liquor Store Agent Compensation

The most recent forecast for liquor sales for the current biennium are coming in higher than the forecast used for the 2021-23 LAB. An increase in expenditure limitation is needed to pay liquor store agents in accordance with a statutory formula through the end of the biennium. Liquor store compensation costs are directly associated with liquor sales. Oregon liquor store agents are contracted by the state to sell liquor. Stores are paid through a formula based on their sales. The compensation formula for liquor stores was set in statute in 2021, through the passage of House Bill 2740. The compensation formula is specific to each of the 283 stores and their sales, with an average rate for all 283 liquor stores expected to be 10.1 percent of gross liquor sales in the 2021-23 biennium.

The 2021-23 LAB is based on a \$1.598 billion forecast, resulting in \$159.1 million of expenditure limitation in the budget for agent compensation. However, based on actual sales for the last 12 months, the revenue forecast for sales is now \$1.691 billion, a five percent increase. The updated forecast results in an anticipated need of \$171.0 million for agent compensation. The difference between the previous forecast and the updated forecast results in an additional

need of \$11.9 million Other Funds expenditure limitation to pay liquor store agent compensation in compliance with the statutory formula.

Distillery Agent Compensation

The most recent forecast for liquor sales by distillery agents for the current biennium are coming in higher than the forecast used for the 2021-23 LAB. The increase is directly related to liquor sales from distillery tasting rooms. Distillery agents are distilleries that contract with OLCC to allow direct retail sales out of their tasting rooms. Prior to the 2021-23 biennium, distillery agents were paid compensation similar to liquor store agents; however, in 2021, Senate Bill 316 changed the compensation formula. Compensation for distillery agents is now 45 percent of annual gross sales up to \$250,000 and 17 percent of sales above \$250,000 occurring within a calendar year. This is estimated to result in an average compensation rate for all distilleries of 37 percent for the 2021-2023 biennium. Distillery agent sales began in 2009 and have averaged 11 percent annual growth over the last five years, primarily due to the increase in the number of distilleries in the state.

The 2021-23 LAB provides \$7.8 million of expenditure limitation for distillery agent compensation. However, based on actual sales for the last 12 months, the revenue forecast has increased to an anticipated \$30.4 million in sales, a 31 percent increase. The updated forecast results in an anticipated need of \$11.5 million for distillery agent compensation. The difference between the previous forecast and the updated forecast results in an additional need of \$3.7 million Other Funds expenditure limitation to pay distillery agent compensation in compliance with the statutory formula.

Legal Reference: Increase Other Funds expenditure limitation established by chapter 640, section 1(1), Oregon Laws 2021, for the Oregon Liquor and Cannabis Commission, Administrative Expenses, by \$2,562,734 for the 2021-23 biennium.

Increase Other Funds expenditure limitation established by chapter 640, section 1(4), Oregon Laws 2021, for the Oregon Liquor and Cannabis Commission, Agents' compensation- all other, by \$11,881,048 for the 2021-23 biennium.

Increase Other Funds expenditure limitation established by chapter 640, section 1(5), Oregon Laws 2021, for the Oregon Liquor and Cannabis Commission, Agents' compensation-distillery agents, by \$3,733,000 for the 2021-23 biennium.



Oregon

Kate Brown, Governor

Liquor and Cannabis Commission

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August 22, 2022

Senator Peter Courtney, Co-Chair
Representative Dan Rayfield, Co-Chair
Joint Emergency Board
900 Court Street NE
H-178 State Capitol
Salem, OR 97301

Dear Co-Chairs:

Nature of the Request: The Oregon Liquor and Cannabis Commission (OLCC) respectfully requests an increase in Other Funds expenditure limitation in the amount of \$18,176,782 to accommodate payments for bank card fees and liquor agents, as a result of increased liquor sale revenue projections.

Agency Action/Need: Gross liquor revenues are expected to be higher than the 2021-23 legislatively adopted budget forecast by \$82.0 million, which creates a projected net benefit of \$22.2 million for the General Fund, cities, and counties. The increase in forecasted sales also drive additional costs for bank card fees, store agent compensation, and distiller agent compensation, all of which are figured as a percentage of sales.

The three specific components of the additional Other Funds expenditure limitation request are detailed below:

1) Increase Bank Card Expenditure Limitation for Liquor Sales:

Bank Card costs have increased significantly above the forecasted legislatively approved budget levels for the current biennium and are expected to exceed the current approved budget limitation.

Additional limitation is needed so that consumers purchasing liquor can continue using credit cards. The increase in costs have come from three sources:

- Total Liquor sales in the 2021-23 biennium are 5% above forecast. In addition, liquor sales to consumers are 8% above forecast. Only consumers can use credit cards for purchasing liquor.
- Bank card usage (percent of purchases using credit cards) rose from 80% to 90% in April of 2022 as a result of the pandemic. The 90% usage of bank cards has been sustained through the current biennium. The legislatively approved budget forecast for bank card expenditures assumed an 80% usage rate which was the rate before the pandemic for liquor purchases.

- Additional costs from our Treasury approved bank card service provider, Elavon. The estimated additional charges for the current biennium are \$374,000 (\$17,800 per month).

Liquor stores in Oregon are provided credit card services by Oregon State Treasury, with those costs being charged to OLCC. Credit card costs for liquor purchases are included in OLCC's Other Funds budget. OLCC forecasts liquor sales and the associated bank card costs associated with those sales 11 months before the start of the biennium and at times need to be updated during the biennium based on updated sales forecasts. Bank card costs associated with liquor sales are a cost of doing business and cannot be directly controlled by the agency. This request is a forecast based on 12 months of actual fees and liquor sales and projected fees and sales for the next 12 months of the current 2021-23 biennium.

2) Increase Liquor Store Agent Expenditure Limitation for Increased Agent Compensation:

The current biennium limitation for 2021-23 of liquor store compensation is \$159,118,952. Liquor sales for the current biennium to date and store agents' compensation costs are running above forecast. An increase in limitation is needed to continue to pay liquor store agents per statutory formula through the end of the biennium. Liquor store compensation costs are directly associated with liquor sales. The updated forecast for liquor store compensation is estimated at **\$171,000,000**, based on 10.1% of forecasted liquor store sales, which is now estimated at **\$1.691 Billion** for the current biennium (6% above the legislatively adopted budget forecast).

Oregon liquor store agents are contracted by the state to sell liquor. Stores are paid with a formula based on their sales. The compensation formula for liquor stores was set in statute in 2021 through the passage of HB 2740. The compensation formula is specific to each of the 283 stores and their sales but the average rate for all 283 liquor stores is expected to be 10.1% of gross liquor sales in the 2021-23 biennium. The current biennium forecast for 2021-23 of liquor store compensation is based on the legislatively adopted budget revenue of \$1.598 billion. The current forecast for liquor sales based on 12 months of actual sales is now \$1.691 billion (5% increase). The formula relies on the variable rates for compensation which are tied to sales.

3) Increase Distillery Agent Expenditure Limitation for Distillery Agent Compensation:

Distillery agent compensation is exceeding forecast through the first 12 months of the 2021-23 biennium. Compensation is directly related to sales from distillery tasting rooms. An increase in limitation is needed to continue to pay distillery agents through the end of the biennium. Compensation is directly related to sales from distillery tasting rooms. Distillery agent sales and compensation are trending at a higher level due to sales above forecast coming out of the pandemic and with the passage of SB 316 in the 2021 session which increased the compensation rate distillery agents receive from tasting room sales. Currently, compensation for distillery agents is forecast to be \$11.5 million. Biennium sales for distillery tasting rooms in 2021-23 are now expected at \$30.4 million which is 31% above the legislatively adopted budget forecast, and 47% above the previous biennium.

Distillery agents are distilleries that contract with OLCC to allow direct retail sales out of their tasting rooms. Previously, these agents were paid compensation similar to liquor store agents, however, in 2021 Senate Bill 316 passed which changed the compensation formula and established it in statute. Compensation for distillery agents is now 45% of annual gross sales up to \$250,000 and 17% of sales above \$250,000 occurring within a calendar year. This is estimated to result in an average compensation rate for all distilleries of 37% for the 2021-2023 biennium. The current legislatively adopted budget limitation that OLCC pays for distillery agents' compensation is \$7,767,000. Distillery

agent sales began in 2009 and have averaged 11% annual growth over the last 5 years primarily due to the increase in the number of distilleries in the state. However, coming out of the pandemic, annual sales have increased to almost 20%.

Action Requested:

1) 2021-23 LAB Limitation for Bank Cards:	\$17,937,266
Forecast Limitation Needed For Bank Cards in 2021-23:	<u>\$20,500,000</u>
Additional Limitation Request for Bank Card Costs:	<u>\$2,562,734</u>
1) 2021-23 LAB Limitation for Store Agents Compensation:	\$159,118,952
Forecast Limitation Needed For Store Agents Compensation in 2021-23:	<u>\$171,000,000</u>
Additional Limitation Request for Store Agents Compensation:	<u>\$11,881,048</u>
3) 2021-23 LAB Limitation for Distillery Agents Compensation:	\$7,767,000
Forecast Limitation Needed For Distillery Agents Compensation in 2021-23:	<u>\$11,500,000</u>
Additional Limitation Request for Distillery Agents Compensation:	<u>\$3,733,000</u>

Total Other Funds Expenditure Limitation Increase Request: **\$18,176,782**

Legislation Affected:

Chapter 640, 2021 Oregon Laws 2021, Section 1(1), Administrative expenses.

Chapter 640, 2021 Oregon Laws 2021, Section 1(4), Agents' Compensation - all other.

Chapter 640, 2021 Oregon Laws 2021, Section 1(5), Agents' Compensation - distillery agents.

Thank you for your consideration

Sincerely,



Steve Marks
Executive Director
Oregon Liquor and Cannabis Commission

CC: Michelle Deister Legislative Fiscal Office
Tamara Brickman DAS/Chief Financial Office