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Is government control of the liquor trade still justified?

October 2005

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Foreword

The commercial monopoly that we see in the Société des alcools du Québec (SAQ) is a vestige of the past with origins going back to the Prohibition era of the 1920s. Putting the government in charge at that time aimed at controlling alcohol consumption. Even though this context is now far behind us, every recent attempt to reform the SAQ has failed. In 1985, Rodrigue Biron, then a minister in the Quebec government, proposed a partial privatization, but this went nowhere. A working committee set up by the government in 1997 examined full liberalization of the sector, but without any more success.

The long strike last winter at the SAQ brought back questions about the pertinence of this type of government monopoly here in the 21st century, at a time when people are allowed increasingly to make their own decisions about how they want to live and what they want as consumers. Similar questions are being raised in other provinces. In Ontario, a committee created by the provincial government to examine how liquor is sold reached the following conclusion in a report released this past July: "Following a six-month review, our Panel has come to the unanimous conclusion that the Ontario government should withdraw from ownership and operation of wholesale and retail beverage alcohol business and instead create a regulated but competitive marketplace."

This study by Valentin Petkantchin looks at several sides of the issue. The author goes over the various arguments that are heard regularly, such as the fact that alcohol is not just another product, and he concludes that none of this reasoning justifies the SAQ's existence. He shows that using government stores to sell beverages not only fails to lower alcohol consumption but ends up penalizing responsible drinkers, meaning the vast majority among us.

This study is also of great interest because it is one of the few studies, if not the only one, providing an idea of the SAQ's performance in relation to the LCBO in Ontario and the privatized system in Alberta. Are we better served by our SAQ monopoly in Quebec than Albertans are by their privatized system? Strange as this may seem, the study uses figures to show not only that privatization puts consumers at an advantage but also that it enables governments to increase revenues from this sector.

It is time to restart a serious debate in Quebec on this issue. This study from the Montreal Economic Institute will most certainly enable everyone to understand this question more clearly.

Michel Kelly-Gagnon
President

Valentin Petkantchin, Research Director, Montreal Economic Institute

Is government control of the liquor trade still justified?

Résumé

Ce Cahier de recherche se penche sur les justifications et les conséquences économiques de la présence d'un monopole d'État au Québec dans le commerce d'alcool. Comme il est expliqué dans la première section, ces monopoles d'État sont des vestiges du passé. Leur origine au Québec, mais aussi dans les autres provinces du Canada, remonte à l'époque peu glorieuse de la prohibition et du régime sec aux États-Unis au début des années 1920.

Même si ce contexte historique n'existe plus depuis longtemps, presque toutes les provinces canadiennes maintiennent un contrôle strict sur les importations, l'entreposage, la distribution et la vente de produits alcooliques. Au fil des années, on a toutefois perdu de vue les objectifs de tempérance qui ont été la justification principale de ces politiques. La Société des alcools du Québec (SAQ) est aujourd'hui devenue un monopole commercial qui garde les consommateurs captifs et qui essaie de se substituer à ce qu'une multitude d'entreprises privées auraient pu offrir dans des conditions de concurrence.

Les gouvernements provinciaux justifient leur mainmise sur ce secteur commercial en invoquant les effets nocifs de l'alcool sur la santé, la dépendance à l'alcool, les coûts sociaux qu'il entraînerait, voire une plus grande efficacité économique. Ce contrôle génère par ailleurs aussi des revenus considérables que les gouvernements craignent de perdre en cas de privatisation.

La deuxième section examine tous ces arguments et montre qu'aucun d'entre eux ne justifie le monopole commercial actuel de la SAQ. Par exemple, le fait qu'il existe des effets nocifs sur la santé dans le cas d'une consommation excessive d'alcool ne justifie en rien l'existence d'un monopole. Les Québécois peuvent se procurer de l'alcool dans les quantités qu'ils désirent, exactement comme cela aurait été le cas en l'absence de monopole. Ce n'est pas parce que les magasins où on achète l'alcool

Executive Summary

This Research Paper deals with the justifications for preserving a government monopoly on liquor sales in Quebec and the economic consequences of this policy. As explained in the first section, these government monopolies are vestiges of the past. Their origins in Quebec and the other Canadian provinces go back to the inglorious days of prohibition and the United States dry laws of the early 1920s.

Even though this historical context long ago ceased to exist, nearly all Canadian provinces maintain strict controls over the import, storage, distribution and sale of alcoholic beverages. Over the years, however, the temperance goals that served as the main justification for these policies have been lost from view. The Société des alcools du Québec (SAQ) has become a commercial monopoly that holds consumers hostage and tries to take the place of what a host of private companies could offer under competitive conditions.

Provincial governments justify their grip on this commercial sector by means of pretexts such as health hazards, alcohol addiction, social costs and even economic efficiency. This control also generates sizable revenues that they fear losing if privatization were to occur.

The second section examines all these arguments and shows that none of them justifies the SAQ's current commercial monopoly. For example, harmful health effects resulting from excessive alcohol consumption hardly justify the existence of a monopoly. Quebecers can obtain alcohol in the amounts they desire exactly as if there were no monopoly. Purchasing bottles in stores belonging to the government rather than to private businesses does not somehow make the health hazards disappear.

Despite the dearth of arguments to justify preserving the SAQ's monopoly, the privatization option remains controversial. Certain studies purport to show that a privatized system would cause governments to lose the dividends from their monopolies (nearly $600

appartiennent à l'État, et non à des entreprises privées, que les effets nocifs pour la santé disparaissent.

En dépit de l'absence d'arguments justifiant le maintien du monopole de la SAQ, l'option de la privatisation reste controversée. Certaines études tentent de montrer qu'avec un système privatisé, les gouvernements perdraient le dividende provenant de leur monopole (qui, pour la SAQ, se chiffre à près de 600 millions de dollars par année) au profit du secteur privé. De plus, selon les critiques de la privatisation, le marché privé fournirait aux consommateurs une sélection moins large de produits, un service de moindre qualité, des prix plus élevés, etc.

La troisième section présente une étude de cas comparant les performances du Québec et de l'Ontario — qui possède un monopole semblable à celui de la SAQ — avec celles de l'Alberta, qui a en grande partie privatisé le commerce des boissons alcooliques au début des années 1990. En dépit du fait que le marché albertain n'a pas été totalement ouvert à la concurrence (l'importation, le commerce de gros et la distribution restant sous le contrôle des pouvoirs publics), les données montrent clairement que la privatisation présente des avantages. Il y a en Alberta trois fois plus de magasins, un niveau semblable de prix des boissons, davantage de produits disponibles et autant de revenus pour le gouvernement, qu'au Québec et en Ontario.

Ni les arguments théoriques, ni les performances économiques ne justifient le maintien du monopole actuel de la SAQ. Il n'existe aucune raison de maintenir une telle attitude paternaliste de la part des pouvoirs publics, visant à dicter aux consommateurs leur style de vie et les boissons qu'ils ont ou non le droit de boire. Ces derniers sont en mesure de faire leur choix en adultes responsables.

Alors que dans les années 1920 le gouvernement du Québec avait certainement la politique de contrôle du commerce d'alcool la plus libérale et la moins néfaste en Amérique du Nord, il se trouve parmi les plus restrictifs en 2005. Il serait temps de discuter des différentes modalités de privatisation de la SAQ et de libéralisation du commerce d'alcool afin de tourner cette page qui remonte à la prohibition.

million a year in the SAQ's case) to the private sector. Critics of privatization also argue that the private market would leave consumers with a narrower product selection, poorer service, higher prices and so on.

The third section presents a case study comparing the performances of Quebec and Ontario (the latter having a monopoly similar to the SAQ) with that of Alberta, which largely privatized the sale of alcoholic beverages in the early 1990s. Although the Alberta market is not fully open to competition, with public authorities maintaining control over the import, wholesale and distribution side, the data show clearly that privatization offers advantages. Alberta has three times more stores, similar prices, more products available and just as much government revenue compared to Quebec or Ontario.

Neither theoretical arguments nor economic performance justify maintaining the SAQ's current monopoly. No reason exists to preserve this paternalistic attitude on the part of public authorities who seek to dictate lifestyles and to tell consumers which beverages they have the right to drink. As responsible adults, citizens are capable of making their own choices.

While in the 1920s the Quebec government clearly had the most liberal and least detrimental policy in North America for controlling the sale of liquor, in 2005 it is among the most restrictive. The time has come to discuss the various ways of privatizing the SAQ and liberalizing liquor sales, turning a page that goes back to the era of prohibition.

Introduction

The strike at the Société des alcools du Québec (SAQ) in the winter of 2004-05 gave us a good illustration of the economic drawbacks of a government monopoly in the liquor trade. It was damaging not only for consumers as a whole, who were taken hostage, but also for the Quebec government, whose revenues were hurt by lost sales at the busiest time of the year. Instead of the higher net profit forecast for the SAQ, earnings were down by about $25 million in 2004-05 compared to the previous year.[1]

The history of government liquor monopolies goes back to the Prohibition era and the dry laws in the United States in the early 1920s. The effects of this Puritanism were similar in Canada, where nearly all provinces have since maintained strict control over the import, storage, distribution and sale of alcoholic beverages. Vestiges of these policies can be found in the very presence of the SAQ.

There no longer exists any reason for maintaining this sort of paternalistic attitude, with government authorities seeking to dictate consumers' lifestyles. Consumers are capable of making their own beverage choices as responsible adults. Although the historical context of Prohibition no longer exists, most provincial governments in Canada continue nonetheless to preserve their monopolies based on arguments about putative advantages in health, economic efficiency and quality of service. Their control over this commercial sector has been a major revenue source that they fear losing in the event of privatization.

It has to be asked if these justifications are well founded and what the real impact would be if the government got out of the liquor business. In the first part, we will present the historical context, without which it is difficult to understand the origins of today's SAQ. In the second part, we will examine the various theoretical arguments that are made in continued support of preserving the SAQ's monopoly. We will conclude by comparing the performances and efficiency of government monopolies (the SAQ in Quebec and the LCBO in Ontario) with the privatized system in Alberta.

The history of government liquor monopolies goes back to the Prohibition era and the dry laws in the United States in the early 1920s.

1. See the article titled "Le bénéfice de la SAQ a légèrement diminué en 2004," *Le Devoir*, p. B3, June 16, 2005.

1. Historical origins of the liquor monopoly in Quebec

It is impossible to understand the SAQ's role and the place it holds without going back to its historical origins, closely linked to the context of Prohibition and the dry laws of the 1920s.

1.1 From Prohibition to the creation of a public sector monopoly in 1921[2]

Prohibition in North America, in Canada as well as in the United States, came about due to efforts by the public authorities to regulate alcohol, going back at least to the mid-19th century. In 1864, the Temperance Act, or Dunkin Act, was adopted by the United Province of Canada, giving municipalities the power to prohibit the retail sale of liquor after holding public consultations. In 1878, the Canada Temperance Act, or Scott Act, modified the law, making it easier to organize and call citywide public consultations.

In 1919, Quebec thus became the only jurisdiction in North America without total prohibition.

In 1898, the Canadian government held a referendum on total prohibition. Although the other provinces voted in favour of prohibition, a lively reaction was felt in Quebec, where it was rejected by a majority of voters. This Quebec specificity in relation to the other provinces drew ample comment at the time in certain newspapers that defended freedom of choice against prohibition. Historian Fernande Roy quotes from the newspaper *Le Prix courant*, which saw prohibition as being "in direct opposition to modern ideas of civic and natural freedom."[3] A widespread view held that the other provinces could not impose their Puritanism on Quebec. Another newspaper, *Le Moniteur du commerce*, called the Act "a monstrous thing, a challenge to individual freedom in a civilized nation."[4] The Catholic Church also opposed the idea of prohibition. In the referendum, 81% of Quebec voters ended up rejecting the prohibition proposal, in contrast to the rest of Canada.

Although a slim majority across Canada supported prohibition, with 51% of votes cast in its favour,[5] prohibition failed to take effect because Prime Minister Wilfrid Laurier chose "to disregard the referendum results, invoking the low popular turnout for the vote, which amounted to just 44% of registered voters."[6]

In 1917, without any new law imposing prohibition at the federal or provincial level, every province except Quebec became "sober" on a town-by-town basis through successive applications of the Scott Act. In Quebec, on February 7, 1918, the provincial government adopted a law calling for total prohibition, intended to take effect on May 1, 1919. Powerful opposition arose, especially with the attempt to prohibit popular products such as beer, wine and cider. In a referendum on April 10, 1919, with the clergy also coming out against total prohibition, a majority across Quebec voted against having the government outlaw beer, wine and cider. "At certain polling stations in Montreal, not a single vote was cast in favour of total prohibition."[7]

In 1919, Quebec thus became the only jurisdiction in North America without total prohibition. The Quebec position was far more rational and modern than what prevailed elsewhere in Canada and in the United States. With the benefit of hindsight, such a policy can be seen unquestionably as a better solution than total prohibition as adopted by our U.S. neighbours between 1919 and 1933. As American economist Mark Thornton notes, the consequences

2. Much of the information here on the history of liquor regulation comes from an SAQ document, *La Société des alcools du Québec et son environnement*, 2nd edition, August 1997, and from a book by Robert Prévost, Suzanne Gagné and Michel Phaneuf, *L'histoire de l'alcool au Québec*, SAQ, 1986.
3. Fernande Roy, *Progrès, harmonie, liberté. Le libéralisme des milieux d'affaires francophones de Montréal au tournant du siècle*, Montreal, Boréal, 1988, pp. 119-120.
4. *Idem*.
5. Ruth Dupré, "The prohibition of alcohol revisited: the U.S. case in international perspective," Research Paper No. IEA-04-11, October 2004, HEC Montréal, p. 11; available at *http://papers.ssrn.com/sol3/papers.cfm?abstract_id=615723*.
6. SAQ, *op. cit.*, 1997, p. 3.
7. SAQ, *op. cit.*, 1997, p. 3.

of this extreme intervention by the U.S. Government were catastrophic from every point of view:

> *Although consumption of alcohol fell at the beginning of Prohibition, it subsequently increased. Alcohol became more dangerous to consume; crime increased and became "organized"; the court and prison systems were stretched to the breaking point; and corruption of public officials was rampant. No measurable gains were made in productivity or reduced absenteeism. Prohibition removed a significant source of tax revenue and greatly increased government spending. It led many drinkers to switch to opium, marijuana, patent medicines, cocaine and other dangerous substances that they would have been unlikely to encounter in the absence of Prohibition.*[8]

These perverse effects were not characteristic solely of the American dry laws. In Quebec, similar effects started to be observed with the partial prohibition of 1919 that banned spirits. "There are many violators, and clandestine outlets are becoming numerous. A major network of illegal distillation of spirits is taking root."[9]

This was the context in 1921 that led the Quebec government to adopt the Alcoholic Beverages Act abolishing partial prohibition. This same Act also founded the Quebec Liquor Commission, the SAQ's forerunner. The law assigned to it "the trade in spirits and wines, and submits the trade in beer to the control of this same Commission."[10] It was handed a number of monopolistic powers: it held a monopoly on any sale of alcoholic beverages in the province; it alone had the right to import and transport them; it controlled all sales of beer and wine through the issuance of permits to hotels, restaurants, taverns, clubs and so on. It also received police powers (pursuing and charging violators of the law anywhere in the province) and surveillance powers over licensed establishments. A surveillance department and a "secret service" were created, with 35 inspectors at the beginning.[11] Compared with prohibition, establishment of a government monopoly was undeniably a better option, but fraud and contraband remained, fed as they were by artificially high prices and the inconvenience a monopoly causes to consumers.

In this context, the following observation in 1924 by the Quebec Liquor Commission itself is hardly astonishing: "Mention has been made in the report of the surveillance department of the importing to this province of contraband liquor produced in the United States. This state of affairs is just one of the manifestations of trouble that is becoming more serious every day, that is threatening to overwhelm, and indeed has already overwhelmed, nearly every branch of the trade, and that constitutes a problem that is extremely difficult to resolve."[12] The only solution to this problem consisted of gradually reducing the severity of restrictions on consumption and having the Commission do what private entrepreneurs were doing: try to satisfy demand from consumers. The result is that having the Commission turn into a commercial monopoly—a monopoly that tries to do what the private market would have done—seemed inevitable.

Compared with prohibition, establishment of a government monopoly was undeniably a better option, but fraud and contraband remained.

1.2 The shift toward a commercial monopoly

With the establishment of a government monopoly, the liquor trade was literally nationalized. "For the Commission, this involved taking the place of several dozen wholesalers and many hundreds of retailers (...)"[13] that endeavoured to satisfy Quebec's demand for alcoholic beverages. The government liquor monopoly appeared to uphold temperance goals at the beginning. The stores did not display merchandise, which was kept hidden behind the counter, and customers had to show a permit in which each purchase was recorded. However, the Commission soon

8. Mark Thornton, "Alcohol Prohibition Was a Failure," *Policy Analysis* 157, July 17, 1991, available at *http://www.cato.org/pub_display.php?pub_id=1017&full=1.*
9. SAQ, *op. cit.*, 1997, p. 3.
10. Commission des liqueurs du Québec, *Rapport annuel de la Commission des liqueurs du Québec 1922-1923*, 1923, p. 49.
11. Prévost *et al.*, *op. cit.*, p. 95.
12. Quebec Liquor Commission, *Rapport annuel de la Commission des liqueurs du Québec 1923-1924*, 1924, p. 7.
13. Quebec Liquor Commission, *op. cit.*, 1923, pp. 49-50.

In a blatant paradox, this commercial orientation destroyed the very justification for the monopoly's creation in 1921.

adopted a more commercial orientation "to ensure the best possible prices to the customer."[14] This shift put commercial and temperance goals in direct conflict. With a commercial monopoly, temperance was effectively pushed into the background. In a blatant paradox, this commercial orientation destroyed the very justification for the monopoly's creation in 1921. If the advantages of a government monopoly seemed obvious in helping ensure temperance as opposed to a competitive private market, this was no longer the case if the goal became one of obtaining the best prices for consumers.

Despite this commercial orientation, nationalization seemed irreversible at the time since the Commission also became a major source of government revenue. As pointed out in a study, "toward 1925, levies on the production, commercialization and consumption of alcoholic beverages accounted for between 19 and 25 per cent of total revenue for the government of any particular province, with this proportion varying by province. In 1925, this proportion reached 23 per cent in Quebec."[15]

The monopoly underwent a number of changes over the years, becoming an increasingly commercial business. Following the logic of business growth, the Quebec Liquor Board, created in 1961, opened its first semi-self-service branch soon afterward, at Place Ville-Marie in Montreal. The Board opened its first fully self-service store in Sherbrooke in 1970. In September 1971, based on a recommendation from the Thinel Commission, the government created two separate entities with distinct responsibilities, one to control liquor permits[16] and the other, in charge of sales, to be called the Société des alcools du Québec (Quebec Liquor Corporation). The newborn SAQ took over the former Liquor Board's 215 branches and its 2,600 employees. Central to this was that "from now on, the role of the Société des alcools du Québec is clearly commercial."[17] The SAQ would continue to pursue an approach based on sales growth. It opened new branches and, over the years, increased the number of products available.

Given the SAQ's commercial vocation, several privatization projects were submitted to the government in the 1980s and 1990s. For example, in 1983, privatization of the SAQ's retail network was announced. The project met fierce resistance from the unions, and attempts to apply it did not get under way until 1985 with the Biron plan calling for 129 branches to be sold. It was to take place through public tenders, but it ended up being cancelled when a new Liberal government came to power in 1986. This privatization project suffered from many weaknesses. It involved privatizing certain points of sale in Montreal but with no competition allowed. Privatized stores would have been sheltered from new competitors. The benefits to consumers of this partial privatization, had it gone ahead, would have been very limited. In the absence of competition, consumers would have remained captive, with no real alternative. Moreover, the remaining SAQ branches would also have been sheltered from competition from the privatized stores, which would have been required to buy their merchandise from the SAQ at fixed prices.

In 1997, a working document was also prepared at the request of the Minister of Finance, suggesting several ways the SAQ could improve "administrative efficiency" in this industry sector.[18] These scenarios ranged from maintaining the status quo to a complete privatization and liberalization of the liquor trade. Comparisons with several U.S. states produced observations of "a continuing shift toward a greater privatization of activities" in the commercial field, and it was found that "the Canadian provinces other than Alberta ranked among the most restrictive in terms of a private presence in the retail trade,"[19] but

14. SAQ, *op. cit.*, 1997, p. 5.
15. André Bernard, "Les politiques gouvernementales en matière de vins et spiritueux au Canada," *Études canadiennes*, No. 35, 1993, p. 19; available at *http://www.afec33.asso.fr/ftp/revue/pdf/n35-a.pdf*.
16. This was the Commission de contrôle des permis d'alcool, later called the Régie des permis d'alcool du Québec and finally the Régie des alcools, des courses et des jeux, its current name.
17. SAQ, *op. cit.*, 1997, p. 10.
18. Working group on the alcoholic beverage sector in Quebec, "Réflexions sur l'organisation du secteur des boissons alcooliques au Québec," consultation document, 1997, p. i.
19. *Ibid.*, p. 23.

the SAQ nonetheless retained its status as a government monopoly.

In contrast to 1921, when Quebec policy was less interventionist than anywhere else in North America, the Quebec government today is among those most heavily involved in the liquor trade. The SAQ, through its monopoly, enjoys "exclusivity in the primary distribution in Quebec of all alcoholic beverages with the exception, essentially, of light cider and of beer bottled in Quebec."[20] This notion of exclusivity conceals monopoly powers with several distinct components.

1.3 The broad scope of the SAQ's monopoly powers

For starters, the SAQ has a monopoly on importing alcoholic beverages into Quebec.[21] Next, the SAQ is the only wholesaler and distributor, supplying the various sales networks (grocery stores, convenience stores, agency stores) and licensed establishments (hotels, bars, restaurants etc.) with wine, spirits and imported beer throughout Quebec.

Consumers are held captive. Apart from domestic beer, the SAQ is the obligatory channel for all alcoholic beverages, enabling it to collect a markup on every product sold. This markup, the source of the dividend paid each year to the Quebec government, is not in any way a profit in the usual economic meaning of the term (a profit is the surplus from a service provided after deducting all expenses). Even if it is similar to a net profit from an accounting standpoint, the "profit" that the SAQ pays to the government is similar in nature, from an economic standpoint, to other federal and provincial taxes and could be called a "monopoly tax." Increasing this "profit" requires only that prices be raised, which can be done under the SAQ's monopoly powers. As former Quebec cabinet minister Rodrigue Biron noted with regard to the dividend, the SAQ does not make a profit but "collects $600 million in taxes."[22]

Finally, the SAQ holds a dominant position in the retail sale of wine and spirits.[23] Even though there are other points of sale not belonging to this state-owned corporation, the other retailers (grocery stores, convenience stores and agency stores) are required to comply with the conditions it dictates. For example, food retailers such as supermarkets and convenience stores also sell wine.[24] However, in the food store network, the product range is strictly limited to products bottled in Quebec (the SAQ Alimentation product range). Food stores are thus not really able to compete with SAQ branches in terms either of product selection or of prices, which are set by the government monopoly. Grocers really end up as mere space providers for the SAQ, which collects its markup along the way as the wholesaler for all products sold in food stores.

Agency stores, unlike other grocery stores, have access to the full range of SAQ products, but they operate under agreements with the SAQ and are generally located in remote areas. Obviously, even though these stores are private, this has little to do with privatization. They continue to get their supplies from the SAQ and sell them under conditions set by the SAQ as the wholesaler. Just like grocery stores and convenience stores, they are in no way able to compete with the government-owned liquor stores.

This all comes down to the fact that the original temperance-based justification for creating a government monopoly in 1921 with the establishment of the Quebec Liquor Commission has been lost in the mists of time. Today's SAQ, on the contrary,

The "profit" that the SAQ pays to the government is similar in nature, from an economic standpoint, to other federal and provincial taxes and could be called a "monopoly tax."

20. SAQ, *Purchasing and Merchandizing Policy*, updated March 31, 2003; available at *http://www.globalwinespirits.com/wximage?/1347415/PROMO_FILE/PMP%20030613.pdf.*
21. Alcohol imports (whether from elsewhere in Canada or from abroad) are the exclusive domain of the provincial government under a federal law, the Importation of Intoxicating Liquors Act.
22. Remarks quoted in "La SAQ est-elle privatisable?," *Le Devoir*, January 15-16, 2005, p. B1.
23. As noted by the Working group on the alcoholic beverage sector in Quebec (p. 2), the market for Canadian beer, which accounts for about half of all alcoholic beverage sales in Quebec and across Canada, is separate from the market controlled by the SAQ.
24. This presence of wine and beer in grocery stores actually weakens the argument for maintaining the SAQ's monopoly as a way of controlling alcohol consumption. Alcoholic beverages are very widely available for those who choose to abuse them. The monopoly is of no use in restraining consumption. On the other hand, it creates economic distortions and affects the well-being of consumers of these products, as we shall see in this study.

is a commercial outfit with monopolistic powers, taking the place of private businesses that could very easily be doing the job. What arguments, then, could justify preserving this commercial monopoly?

The original temperance-based justification for creating a government monopoly in 1921 with the establishment of the Quebec Liquor Commission has been lost in the mists of time.

2. Arguments that fail to justify the SAQ's monopoly

A number of theoretical arguments have been put forward to justify preserving a government monopoly like that of the SAQ in the liquor business.

2.1 Alcohol is not just another product

The argument heard most often whenever the issue of privatization comes up is that alcohol is not just another product—for two main reasons.

First, alcohol is not just another product because it presents health risks, according to a common line of reasoning that often comes with a long list of diseases related to alcohol consumption. "Alcohol is not just another consumer product. It contributes to a wide range of health and social problems... such as liver cirrhosis, cancers and addiction."[25]

However, the fact that alcohol may cause serious illness hardly justifies the SAQ's monopoly. To begin with, what is presented solely as a medical argument also has a broad economic aspect. Economic analysis examines individual choices, and consumers are thought to know best whether or not they prefer to drink alcohol. Even if there are health risks, consumers take these potentially dangerous effects into account and add them to the monetary costs they must pay to drink alcoholic beverages. This means they decide to consume alcohol if the satisfaction they get from it—and only they can ascertain this—is greater than all monetary costs and health risks.

The health risks connected with alcohol hardly make it unique: many other goods and activities cause health risks without being placed under a government monopoly. For example, knives and other sharp objects present very obvious potential dangers, and yet nobody is suggesting that they should be sold only in government-owned stores. What interests economists is the undeniable fact that alcohol consumption creates satisfaction for some people and that they are prepared to assume its risks and costs. As noted by economist Douglas Whitman, "there is no objective ground for concluding that alcohol consumption is an undesirable choice... The fact that an activity involves costs or sacrifices for individuals does not imply a need for regulation of that activity."[26]

Moreover, this medical argument is even less pertinent, because the harmful nature of alcohol consumption is not clearly recognized even within the medical profession, particularly when consumption remains moderate. For example, many studies show that moderate consumption does not increase, but actually reduces, certain health risks.[27] It may have positive effects, especially for middle-aged people. For example, according to one American study, "alcohol acts as an anti-cholesterol drug, and epidemiological evidence suggests that moderate drinking is associated with reduced mortality from heart disease and stroke."[28]

Even Educ'alcool, a body officially supported by the Quebec government and financed in part by the SAQ, states in one of its own publications that alcohol in any product (wine, beer or hard liquor) can have beneficial effects: "Scientific research shows

Even if there are health risks, consumers take these potentially dangerous effects into account and add them to the monetary costs they must pay to drink alcoholic beverages.

25. See "Retail Alcohol Monopolies and Regulation: Preserving the Public Interest," Position Paper, Centre for Addiction and Mental Health, October 2004; available at *http://www.camh.net/public_policy/retailalcoholmonopolies.html*.

26. Douglas Glen Whitman, *Strange Brew, Alcohol and Government Monopoly*, The Independent Institute, 2003, p. 30.

27. See *http://www.healthydrinkingscience.com/archive.html* for a list of studies showing the positive health effects of moderate alcohol consumption.

28. Philip J. Cook, Jan Ostermann and Frank A. Sloan, "Are Alcohol Excise Taxes Good For Us? Short and Long-Term Effects on Mortality Rates," National Bureau of Economic Research, February 2005, p. 3; available at *http://www.nber.org/papers/w11138*. Also see Dale M. Heien, "Are Higher Alcohol Taxes Justified?," Cato Journal, Vol. 15, Nos. 2-3, Fall-Winter 1995-96; available at *http://www.cato.org/pubs/journal/cj15n2-3-7.html*. Heien writes: "Because it is impossible to levy taxes solely on abusers, tax increases will cause welfare losses for moderate drinkers."

Risks connected with excessive drinking do not vanish because a store where beverages are purchased belongs to the government rather than to a private business.

that, for most people, regular, moderate drinking, i.e. one or two drinks a day, can provide some protection against cardiovascular disease, peripheral vascular disease, type 2 diabetes and gallstones. It can also have a positive impact on a person's psychosocial condition and reduce the risk of rheumatism, arthritis and kidney stones."[29]

Even if it were clearly established that alcohol is harmful, this would not justify having a monopoly because it fails to reduce this harm in any way. The SAQ behaves just like any other commercial business, with temperance no longer a priority. Any consumer can go out and get alcohol in the quantities he or she desires, just as if there were no monopoly. Risks connected with excessive drinking do not vanish because a store where beverages are purchased belongs to the government rather than to a private business, which is the case in most European countries.

Second, the argument that alcohol is not just another product extends to the dependence linked to its consumption. Although this is a real concern in cases of abusive drinking, it is no more of a justification for the SAQ's commercial monopoly. The existence of a monopoly is of no use to people who become dependent on alcohol. They can get the quantities they desire just as easily as in a privatized market.[30] On the other hand, government control over the liquor trade causes harm to many people who drink alcohol without developing a dependency and who are unjustly penalized in terms of higher prices, poorer selection, and so on.

2.2 Alcohol consumption creates externalities or social costs

This strictly economic argument suggests that drinkers fail to take into account the drawbacks and costs they may inflict in due course on other members of society. These "social" drawbacks may take several different forms, as described by economist Douglas Whitman: "The consumption of alcohol creates negative externalities: costs borne not by the consumers of alcohol but by other people in society. Drunk drivers create risks on the road; people suffering from alcohol-related illnesses rely on public health systems; alcoholics are sometimes less reliable and less productive on the job; and so on."[31]

On the one hand, alcoholics are said to be less productive and thus to represent a cost for society. This reasoning is often used to show the economic costs to society caused by alcohol consumption. Although real, these costs are incurred in the private market by individuals themselves. People who are less productive or often absent would normally receive lower remuneration, meaning that neither employers nor society as a whole would have to cover the full cost of their irresponsible behaviour. But even if drinking were the cause of such declines in productivity, the fact that a government monopoly sold the drinks hardly eliminates the phenomenon of abusive drinking.

On the other hand, a variant of the social cost argument consists of emphasizing the financial onus of drinking-related health problems. Alcoholics, it is argued, require more medical attention and are a burden on the health care system. This argument neglects, however, to mention that these external costs exist only to the extent that the health care system is public as in Canada. In a private system, individuals would either pay for their own care (which would force them to take more responsibility for the costs of their drinking) or they would pay higher insurance premiums because of the high long-term insurance risk they would present. As noted by Whitman, "Medical expenses created by drinking and other personal choices are not *unavoidably* external costs—they only become so because of government policies that spread such costs out over the public.[32] In a more fundamental

29. See "The health benefits of regular and moderate consumption of alcohol," Alcohol and health, Educ'alcool, 2005, p. 2; available in English at *http://www.educalcool.qc.ca/cgi/upimages/EducFiles/alcool_et_sante_abr_ang.pdf*.
30. In reality, more than half the alcohol consumed in Quebec comes from beer sales in a privatized market. It is obvious that anyone who wishes to can, and in fact already does, buy alcohol outside the SAQ monopoly.
31. Whitman, *op. cit.*, p. 30. Canadian economist Greg Flanagan also uses this argument; see his study, "Sobering Result: The Alberta Liquor Retailing Industry Ten Years after Privatization," Canadian Centre for Policy Alternatives and Parkland Institute, June 2003, pp. 28-29; available at *http://www.ualberta.ca/~parkland/research/studies/sobering-result-final.pdf*.
32. Whitman, *op. cit.*, p. 33.

sense, even if these social costs well and truly exist because the Quebec health care system is public, they are in no way eliminated or reduced by the existence of the SAQ's commercial monopoly.

The external cost argument comes up in a different form: alcohol may lead to external costs because of the higher risk of being the victim of a highway accident or of being subjected to alcohol-driven criminal behaviour. This argument has a certain validity but, once again, having a government monopoly does not solve this problem: it is impossible to tell the difference between purchases related to responsible drinking and purchases that could lead to criminal behaviour. These risks are just as real in a commercial monopoly system with alcohol available in the desired quantities as they are in a private system. In any event, it would be better for the government to apply measures aimed at restraining alcohol abuse (for example, driving a motor vehicle under the influence of alcohol) or at protecting personal security and property than to be looking after the liquor business.

2.3 A government monopoly keeps fraud and contraband away

This argument suggests that entrusting liquor sales to a government monopoly provides for better control over the stores and eliminates fraud and contraband. This argument relies on issues of bureaucratic management to deal with a problem created exclusively by previous regulations. It should not be forgotten that these problems appeared and became worse because of Prohibition and the temperance policies of the 1920s.

The reality is that a black market exists solely because governments since the Prohibition era have artificially inflated the prices of alcoholic beverages on the legal market through excise duties, high markups and taxes of every sort. As one study indicated, "The share of the various tax levies in the price of alcoholic beverages has made the clandestine production and sale of these very beverages extremely lucrative." [33]

33. Bernard, *op. cit.*, p. 13.

Fraud and contraband should be included among the perverse effects of the tax and regulatory measures that apply to alcoholic beverages rather than as something intrinsic to the liquor trade. Any product subjected to similar regulation and tax treatment would be a target for contraband and fraud. If the aim is really to eliminate them effectively, the solution is to reduce the tax and regulatory burden rather than to strengthen monopoly control. The Liquor Control Board of Ontario estimates that nearly $450 million in liquor sales took place on the black market in 2004,[34] or about 6% of all sales in Ontario. The SAQ estimates that the revenue shortfall from liquor sales outside its network at between $70 million and $100 million per year.[35]

A black market exists solely because governments since the Prohibition era have artificially inflated the prices of alcoholic beverages on the legal market through excise duties, high markups and taxes of every sort.

2.4 The monopoly is a source of government revenue

According to this argument, the government monopoly is legitimized by the substantial dividends that go into government coffers. Like the other arguments, this one has a number of weaknesses. First, it is absurd to find ultimate justification in a professional activity or public policy because of the revenues that happen to go to the government. Should we be drinking more so that the government can garner additional revenues? On the contrary, the purpose of the liquor trade is not to generate revenues for the public treasury but to respond to the needs of vast numbers of Quebec consumers who gain satisfaction from drinking alcoholic beverages.

Next, even if there were an agreement on the absolute need for the government to collect revenues of the magnitude it achieves with the SAQ, a public sector monopoly would not have any greater justification. The government could get just as much revenue from taxing the sales of alcoholic products while leaving the business of selling them to the private sector in a competitive environment. As we shall see further along, the example of Alberta,

34. LCBO, *Annual Report 2003-04*, p. 12; available at *http://www.lcbo.com/images/pdfs/lcbo_an_report.pdf*.
35. See the article by Jacques Benoît, "La SAQ perd de 70 à 100M $ par an," *La Presse*, May 30, 2005.

which privatized retail sales, proves that it is possible, relatively speaking, to get comparable or even higher revenues.

The arguments put forward to legitimize a government monopoly in liquor sales largely fail to justify maintaining the existence of the SAQ. However, certain fears arise in moving ahead with a true privatization for various practical reasons. It is suggested that a monopoly ensures more efficient management of the liquor trade, that the private market would tend to reduce the number of products available and the number of stores, or that it would create an explosion in the sale and consumption of alcohol. Do these fears have a real basis? How do government monopolies stand up to a privatized system?

3. Case study: Quebec, Ontario and Alberta

Economic theory shows how the absence of competition and the establishment of legally protected monopolies generally result in a deterioration of the goods and services offered to consumers. Monopolies have fewer incentives to seek improvement than do businesses that have to compete. Efforts and resources that could go into enhancing the products and services offered to consumers go instead toward pressuring public authorities and toward protecting themselves and preserving the status quo. In the liquor trade, absence of competition could be expected to produce results such as a narrower product range and poorer service to consumers in matters such as density of the store network.

Like the SAQ, the Liquor Control Board of Ontario (LCBO) is a government monopoly, created in 1927.[36] Until recently, Alberta also had a government monopoly, the Alberta Liquor Control Board (ALCB), dating back to 1924. Like the SAQ and LCBO, the ALCB controlled the liquor business—choosing store locations, products to be sold, prices, opening hours and so on. But since 1994 the retail trade has been extensively liberalized and is run by private stores. (On the other hand, importing,[37] wholesaling and distribution remain under the control of public authorities.) The 1993-94 privatization in Alberta has been well documented and analyzed in a number of publications.[38] Our aim here is not to repeat the details of this reform but to emphasize the economic impact of privatization and to compare the performance of a privatized system with the government monopolies in Quebec and Ontario.

The main difficulty in making comparisons arises from the fact that the statutory and regulatory roles of the various boards differ from province to province. It is nonetheless pertinent, taking account of these differences, to compare the SAQ and LCBO with the situation in Alberta, based on the following factors: i) the number of stores, ii) the choice and number of products available in each province, iii) dividends paid to governments, iv) prices; and, finally, v) changes in alcohol sales, to see if they run wild in a private system.

3.1 The number of stores

What effect could privatization of the SAQ be expected to have on the number of stores?

When the total number of stores is tallied up, Alberta, with its private stores, comes out well ahead of Quebec and Ontario with their SAQ and LCBO branches. In 2004, Alberta had 1,087 stores,[39] while Quebec had 801 (398 branches and 403 agency stores)[40] and Ontario had 779 (598 branches and 181 agency stores).[41]

36. For the Ontario system, see the recent report of the Beverage Alcohol System Review Panel titled "Strategy for Transforming Ontario's Beverage System," July 2005; available at *http://www.beveragealcoholreview.on.ca/en/report.htm*.

37. The monopoly on liquor imports (whether from elsewhere in Canada or from abroad) was maintained by the public authorities in Alberta, in compliance with a federal law, the Importation of Intoxicating Liquors Act.

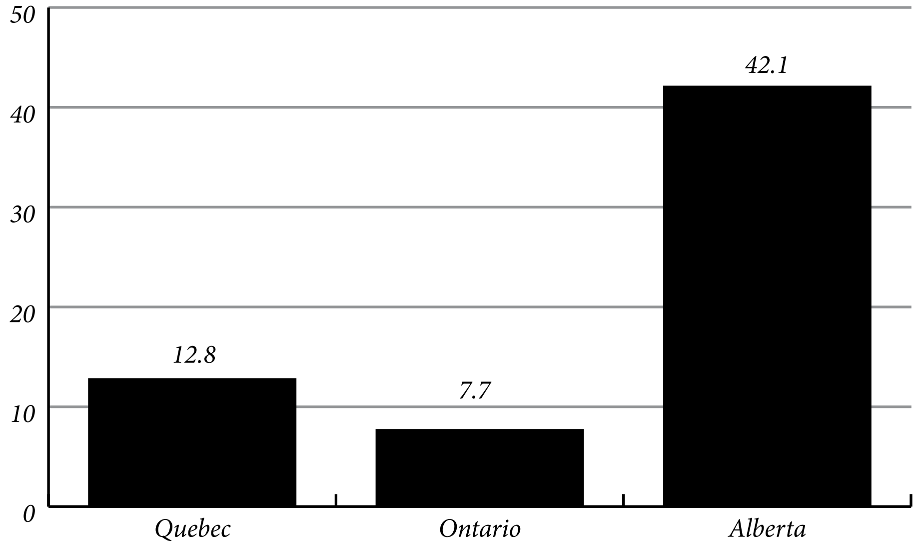
38. See, among other documents: Alberta Liquor Control Board, *A New Era in Liquor Administration: The Alberta Experience*, December 1994; available at *http://www.aglc.gov.ab.ca/pdf/A_New_Era_in_Liquor_Administration.pdf*; Douglas West, "The Privatization of Liquor Retailing in Alberta," Fraser Institute, February 2003; available at *http://www.fraserinstitute.ca/shared/readmore.asp?sNav=pb&id=474*; Greg Flanagan, *op. cit.*; and, Martin Poirier and Martin Petit, "Les impacts de la privatisation de la vente des produits de l'alcool en Alberta," Institut de recherche et d'information socio-économiques, 2003; available at *http://www.iris-recherche.qc.ca/docs/ALCB.pdf*.

39. Alberta Gaming and Liquor Commission, Quick Facts, 2005, available at *http://www.aglc.gov.ab.ca/pdf/quickfacts/quickfacts_liquor.pdf*; figures for January 2005.

40. SAQ, *Annual Report 2004*, p. 58, figures for 2004 available at *http://www.saq.com/img/ent/rapport04/en_pdf/General_Statistics.pdf*. Convenience stores and grocery stores also sell wine, but because they have access to very few products, they cannot be considered on the same footing as SAQ branches.

41. LCBO, *Annual Rreport 2003-04*, p. 14, figures for 2004 available at *http://www.lcbo.com/images/pdfs/lcbo_an_report.pdf*. Other stores, such as The Beer Store outlets

Figure 1 ~ Stores per 100,000 inhabitants (ages 15 and over)



Sources: Annual reports (SAQ, LCBO and AGLC); Statistics Canada, Population by sex and age (data for ages 15 and over), available at *http://www40.statcan.ca/l01/cst01/demo31a.htm*; calculations by the author.

A higher density presents obvious advantages to consumers, who require less time and effort to obtain alcoholic beverages.

This difference in sales network density is even greater if we consider the number of stores per 100,000 inhabitants (see Figure 1). The density is more than three times higher in Alberta than in Quebec and more than five times higher than in Ontario. (The SAQ has a higher density than the LCBO.)

A higher density presents obvious advantages to consumers, who require less time and effort to obtain alcoholic beverages. Economist Douglas West notes that "with the larger number of liquor stores in Alberta, there is improved accessibility, which implies lower transportation and shopping costs, on average, for Alberta consumers."[42] In any assessment of the impact of privatization, it should not be forgotten that time savings can be an important consideration for consumers. The evidence points to a major gap in the performance of a government monopoly, whether in Quebec or Ontario, compared to a privatized system. The latter provides greater consumer satisfaction.

Differences between the private market and a government monopoly amount to more than just a matter of quantity. The basic issue is whether the number of stores is chosen efficiently and whether it matches what consumers want. In Alberta, the opening or closing of a store is left up to private entrepreneurs. They check demand continuously, and it is consumers who end up deciding on store locations by choosing where to shop.

As a result, the number of stores is dictated by consumer demand rather than being planned centrally by a government monopoly. The existence of private stores provides for flexibility and adaptation in the retail network. Some stores disappear and new ones open based on changing market conditions (consumer tastes, technological change that lowers storage and transport costs, urban development, etc.). Exemplifying the dynamism of the private market in Alberta, "at least 28 liquor stores closed from September 1993 to December 1995, 78 closed from December 1995 to January 1998, and 151 from January 1998 to December 2001."[43] Despite these closings, the total number of stores in the province more than tripled in ten years compared to the situation before privatization (see Table 1).

This increase in the number of private stores has generated many new jobs. Employment levels rose considerably in Alberta between 1993 and 1996, going from

and stores at wineries, cannot be compared to LCBO branches.

42. West, *op. cit.*, p. 12.

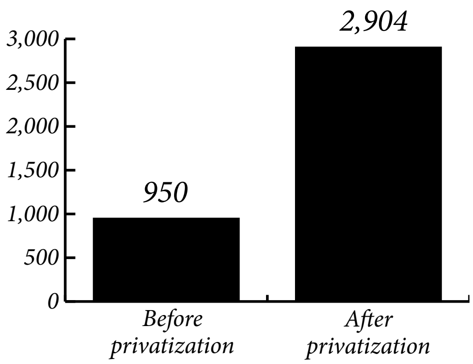
43. West, *op. cit.*, p. 8.

Table 1 ~ Privatization and changes in the number* of stores in Alberta, 1993-2005

Alberta	1993 (September)	1994 (September)	2000 (March)	2002 (March)	2004 (March)	2005 (January)
ALCB branches	202	–				
Beer stores	30	–				
Wine stores	23	–				
Stores at breweries and wineries	6	6	n/a	n/a	n/a	n/a
Agency stores	49	89	77	81	89	91
Private stores	–	486	807	863	950	996
Total	310	575	884	944	1,039	1,087
Increase	–	+85.5%	+185.2%	+204.5%	+235.2%	+250.6%

Source: ALCB, 1994, p. 14; AGLC, *Annual reports,* 2000-2004; AGLC, *Quick Facts*, 2005.
* These figures do not include hotel shops which increased slightly in number after privatization.

Figure 2 ~ Assessment of employment levels in full-time equivalent positions between 1993 and 1996 in Alberta



Source: Douglas West, 2003.

the equivalent of 950 full-time positions to 2,904,[44] more than triple the earlier figure (see Figure 2). This increase in the number of stores was also possible thanks to the fact that wages, which are artificially high in protected monopolies, could be adjusted after privatization to levels comparable to those found in other parts of the retail sector. The work involved in stocking shelves with bottles of olive oil or with bottles of wine is basically the same.

It is hard to deny that full-time unionized employees in a government monopoly, who enjoy advantages in wages and working conditions compared to other retail workers, are directly affected by privatization of the liquor trade. This point should not hide the positive results that a privatization of the SAQ would produce for Quebec consumers as a whole, with more stores at their disposal and the probable creation of many jobs.[45] It remains possible to plan programs to facilitate the transition of employees in government-owned stores to private stores or to other types of business.

Employment levels rose considerably in Alberta between 1993 and 1996, going from the equivalent of 950 full-time positions to 2,904.

3.2 Product selection and quality of service

Product selection and quality of service are two other tests of a commercial operation's performance. It hardly needs pointing out that a lavish product range offers advantages to consumers, responding to their preferences more closely and more effectively. With greater choice, each consumer is better able to find something he or she wants. However, a broader range also creates additional costs in storage, inventory, management of in-store sales space, and so on. The same is true of customer service. A better trained sales staff is able to give better advice to customers, but this also has a cost that customers may or may not be willing to pay and may or may not

44. West, *op. cit.*, pp. 57-59. See AGLC, *op. cit.*

45. Even Quebec critics of the Alberta experience, such as Poirier and Petit, p. 65, feel there has been an increase, albeit more modest, in employment due to privatization in that province.

want. In a market setting, private entrepreneurs are the decision-makers who continuously watch what consumers want. This is what their profit depends on. They are better able than anybody to offer product diversity and service levels based on costs that consumers are prepared to cover. Unlike public sector monopolies, private entrepreneurs satisfy all market niches by diversifying.

Unlike public sector monopolies, private entrepreneurs satisfy all market niches by diversifying.

Does it make sense to believe that in the liquor trade, unlike what can be observed in other lines of business, privatization would end up producing a narrower selection, fewer products available and poorer customer service? We often hear it said that a monopoly provides better customer service because, for example, SAQ employees are better trained than those in the private market and are better able to offer advice. Although there are no quantitative measures to provide for comparisons in quality of service, this argument does not stand up. You cannot have it both ways: consumers either want better service and are willing to pay the cost, in which case the private market will not hesitate to provide it, or they don't require it, in which case it is not economically justifiable to have needlessly overtrained sales staff. Unlike the cookie-cutter approach of a public sector monopoly, all sorts of stores can be observed in the private market with different levels of customer service—from small stores to big specialized ones where expert advice is available—so that all consumers can be satisfied.

Some authors suggest that privatization would also lead to a narrower beverage selection than in a government monopoly system.[46] This line of criticism is based on an indicator (the average number of products per store) that may make sense in the context of a public sector monopoly that always offers the same products, but it has no economic logic in a privatized system like Alberta's. In the private market, stores truly become specialized. One may sell more Bulgarian wines, while another may offer connoisseurs of Australian wines a wider choice and yet another may provide a broader range of Italian wines (because it is located in an Italian immigrant neighbourhood), and so on. This type of specialization creates added value in the eyes of local consumers and in no way means that the average number of products per store has to be higher than in the case of a monopoly that offers the same range everywhere. The number of listings may be lower, but what is important from an economic standpoint is that the selection may vary based on the tastes of local customers. In a market like this, obviously there are also stores that specialize in offering an extremely broad product range. In Calgary, for example, there are stores offering nearly 4,200 different products, far more than the selection offered before privatization in the best top-end government stores (with 2,600 products)[47] or the full range of the LCBO (3,449 products).

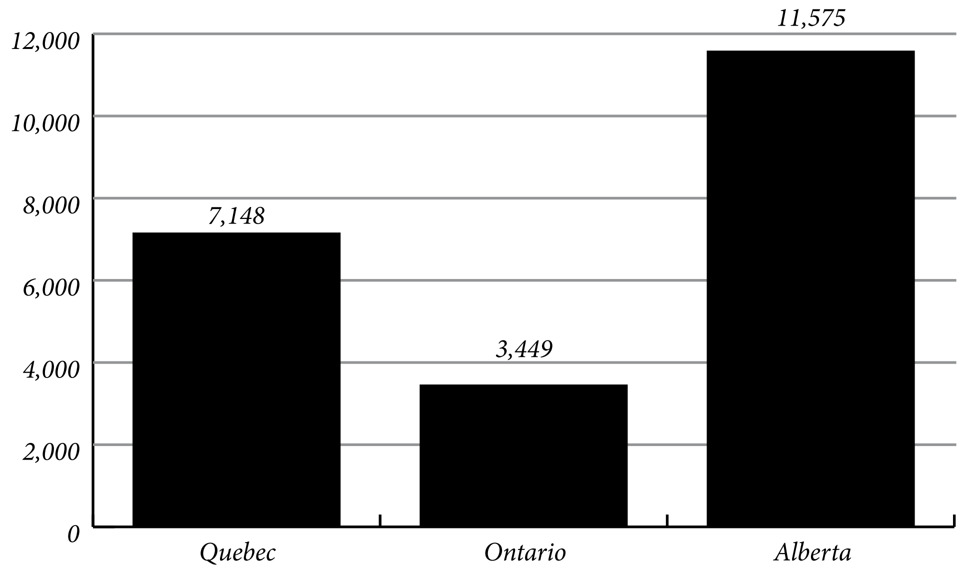
In a private system, the situation is radically different from government monopolies. The private stores choose the products they wish to offer, and they have an incentive (their profits depend on it) to offer products that consumers are looking for. As one study points out, "One of the advantages of the private system is that vendors aren't forced to take a one size-fits-all approach"[48] to product selection. It is completely useless to stock every product available on the provincial market and to display them in each store where alcohol is sold because that represents a cost to retailers. In Alberta, one can observe a diversification "of liquor stores to match any product niche."[49] In the final analysis, comparing the average number of products per store has little economic significance. No store, no matter what it sells (shoes, computers, televisions, etc.), offers every brand and every model available on the market.

The true indicator of product selection or range is the number of products available on the provincial market. The number

46. See, among others, Poirier and Petit, *op. cit.*, p. 30, who find that in Alberta after privatization, "the average number of products per store diminished slightly by 2%."

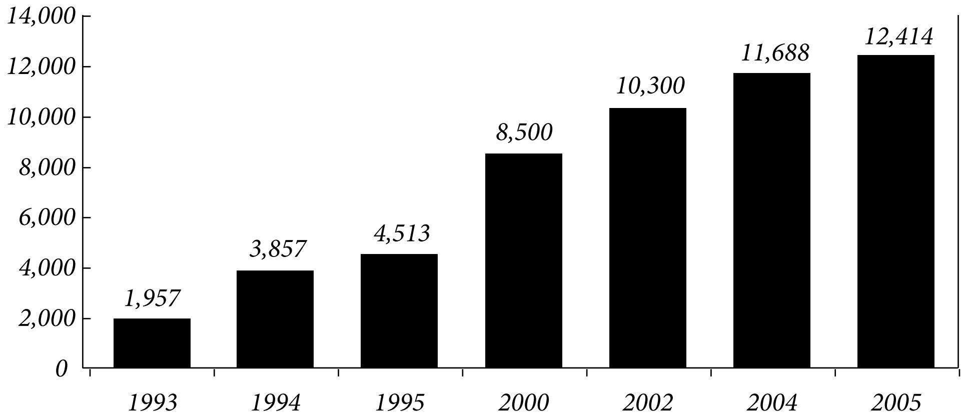
47. See West, *op. cit.*, p. 44.
48. D. MacLean, "Embracing Competition: Recommendations for Reforming Liquor Retailing in Saskatchewan," Canadian Taxpayers Federation, Saskatchewan Division, November 2004, p. 7; available at *http://www.taxpayer.com/pdf/Sask_Liquor_Report_(November_2004).pdf.*
49. *Idem.*

Figure 3 ~ Number of alcoholic products available SAQ, LCBO and AGLC in 2004



Source: SAQ, *Annual Report 2004*, p. 58; LCBO, *Annual Report 2003-04*, p. 44; for Alberta, data obtained upon request from the St. Albert warehouse exclude Canadian beers.

Figure 4 ~ Change in the number of alcoholic products Alberta, 1993-2005



Sources: West, *op. cit.*, p. 45; Annual reports, AGLC.

The private stores choose the products they wish to offer, and they have an incentive (their profits depend on it) to offer products that consumers are looking for.

of alcoholic beverages listed by the various provincial boards or monopolies in their role as wholesalers has more to do with the breadth of product selection than does the average number of products per store. As shown in Figure 3, the SAQ's selection compares favourably to the LCBO's. There is, however, a major gap with the number of listings available in Alberta, which has abandoned control of product selection, and the SAQ and LCBO, which maintain controls.

This difference is explained by the fact that the product selection process differs greatly between a monopoly system and a privatized system. After privatization in Alberta, obstacles to listing a new product were eliminated, and the number of products available in warehouses experienced spectacular growth, going from about 2,000 in October 1993[50] to more than 12,400 in 2005 (see Figure 4).

With privatization, once a supplier is ready to cover the markup paid to the control board, along with the costs of delivery, storage and handling, and once

50. This figure does not include products on agents' lists that were not available for sale in branches. They were sold to permit holders (bars, restaurants, hotels etc.) and numbered 1,221 (see West, *op. cit.*, p. 46).

Table 2 ~ Provincial dividends from alcohol sales in 2002-03

	Sales volume of absolute alcohol[a] (thousands of litres)	Dividends from alcohol sales[b] (thousands of $)	Dividend per litre of absolute alcohol sold
SAQ	23,051[c]	540,000	**$23.43 / litre**
LCBO	41,629	975,000	**$23.42 / litre**
Alberta	21,432	520,667[d]	**$24.27 / litre**

a) This figure is calculated based on real sales by the SAQ, LCBO and AGLC following the methodology used by Statistics Canada.
b) This figure includes only dividends drawn from the public sector monopoly on alcohol sales and does not include other revenues such as those from licences and permits, fines, sales (which would continue to apply whether in the case of a monopoly or of private retailers), etc.
c) This figure does not include domestic beer in Quebec, which is sold outside the government monopoly.
d) This figure includes the AGLC's profit, less the operating costs of its alcohol trade division.
Sources: Statistics Canada, *"The Control and Sale of Alcoholic Beverages in Canada*," 2004; *SAQ, LCBO* and AGLC annual reports for 2002-03; calculations by the author.

Privatizing the SAQ would undeniably let Quebec consumers discover and taste products that are currently unknown to them.

it finds retailers who wish to offer its products, the retailers can have access to these products and decide whether consumers are interested. If retailers make correct decisions, they will end up with profits; otherwise, they risk finding themselves with unsold products on their hands. The competitive market process allows for consumer preferences to be discovered and for the alcoholic beverage selection to be adapted accordingly.[51]

Government monopolies still maintain high barriers to the entry of new products. The administrative procedure is irksome, with various committees, as at the SAQ, that decide instead of consumers what products can be allowed entry to the provincial market.[52] Similarly, in Ontario, "the LCBO's listing practices limit the availability of niche products."[53] The private market, in contrast, provides for far greater flexibility and adaptive capacity, and new products can be made available for sale more easily.

The SAQ keeps consumers captive and limits product listings in its role as wholesaler so as to facilitate management in its retail operations. The result is a narrower product range for consumers than would be available in a private system where competing businesses respond to all market niches. Privatizing the SAQ would undeniably let Quebec consumers discover and taste products that are currently unknown to them.

3.3 Dividend payments to governments[54]

Control over the liquor trade is a major revenue source for provincial governments in the forms of taxes, duties and dividends. There have been fears that privatization could deprive the Quebec government of this assured revenue source, in particular the dividends it receives as the owner of a public sector monopoly. These revenues reached $545 million in 2004-2005. It might be thought that, if this lucrative

51. The ALCB explains this change as follows: "The ALCB has abolished all requirements related to product listing except the need for all products to meet health and labelling standards and regulations. Additionally, product performance is no longer a concern of the ALCB… [I]t has become unnecessary for the ALCB to continue to make decisions on the ability of products to be successful in the marketplace. Under the new model of liquor retailing, producers and retailers determine which products—on both a brand and package size basis—will be sold in which stores, in which areas of the province, at whatever prices suppliers and retailers wish to charge. Consumers, in turn, decide which stores they will patronize, depending on product selection, price and service." (ALCB, *op. cit.*, p. 32).
52. At the SAQ, for example, products must be inspected, in particular by a blind tasting committee and a marketing committee—see SAQ, *Purchasing and Merchandising Policy*, updated March 31, 2003, p. 16, available at *http://www.globalwinespirits.com/wximage?/1347415/PROMO_FILE/PMP%20030613.pdf.*
53. Report of the Ontario Beverage Alcohol System Review Panel, *op. cit.*, p. 2.
54. The issue of other sales taxes that provide revenues to provincial governments is a different matter that should not be confused with dividends drawn from the liquor business. Taxes can just as well be collected in a private sales system as in a public one.

trade were privatized, these profits would go to private business rather than into government coffers.

Whatever the justification—legitimate or illegitimate—of this fiscal burden imposed by the government on the liquor trade, such statements are incorrect. The government can still collect its revenues even with the liquor business in private hands, as is the case in Alberta, where public authorities impose a single provincial tax (called a flat markup) based on the alcohol content of each beverage sold. Contrary to what may be thought, public authorities in Alberta collect more from liquor sales in the form of dividends than the Quebec and Ontario governments obtain with their respective integrated monopolies (see Table 2).

The SAQ sold spirits, wines, imported beers and other beverages containing a total of about 23 million litres of absolute alcohol[55] in 2002-03, more than the total amount of alcohol sold in Alberta. The $540-million dividend means the Quebec government took in about $23.43 per litre of absolute alcohol, or 3.6% less than the Alberta government. In Ontario, the dividend per litre of alcohol sold is almost the same as in Quebec.

The use of these indicators provides for a more realistic comparison between the dividends of the different provinces, despite regional variations in alcohol consumption (for example, Quebecers tend to drink more wine than Albertans do). It also takes account of regulatory differences between the provinces, for example the fact that in Quebec the SAQ's dividend does not include revenues from the sale of domestic beer,[56] unlike Alberta. This means that, if we also removed revenues and quantities connected to the sale of domestic beer in Alberta, given that beer is far more lightly taxed than spirits or wine, its average dividend per litre of alcohol would climb to $30 per litre, nearly 30% more than in Quebec or Ontario. Thus, for example, the Alberta government would have pocketed many tens of millions of dollars more with the SAQ's sales level than the Quebec government collected from its liquor monopoly. It can be seen, then, that the Alberta government gets just as much, or even more, in dividends from the liquor trade with a privatized system than Quebec and Ontario do with their government monopolies.

Unlike the SAQ or LCBO, the Alberta board does not have to assume all the operating risks as a wholesaler and retailer managing warehouses and several hundred branches. Alberta's Gaming Minister, Ron Stevens, stated in 2003: "This year we will be making $550 million or thereabouts from liquor. We no longer have a bunch of real estate that we are responsible for, we no longer have to buy and store liquor... I mean, all those things are direct advantages. We have a lot of businesses that are paying tax whereas before those businesses did not exist."[57] In addition to revenue from the sale of alcoholic beverages, Alberta receives corporate taxes from the many newly created private businesses, unlike the Quebec government, which deprives itself, for example, of the tax on the SAQ's profits in its role as a state-owned monopoly.

To these normal revenues must obviously be added the amounts the Quebec government would get from the sale of SAQ assets in a privatization, with items such as buildings, land, equipment and rolling stock going on the block. For example, the Alberta government sold assets worth more than $59 million in November 1994. As noted by the ALCB, "Revenues [from privatization] have exceeded the initial estimate of $50 million by $9 million."[58] Among these assets were 133 properties with a real property book value of $63.5 million. These properties were sold for more than $50 million during the bidding process, or more than 78% of their book value. On the other hand, 22 properties did not find buyers.[59]

In a privatization, the government could also try to sell the goodwill of the state-

Public authorities in Alberta collect more from liquor sales in the form of dividends than the Quebec and Ontario governments obtain with their respective integrated monopolies.

55. This is a concept used by Statistics Canada, "The Control and Sale of Alcoholic Beverages in Canada," 2004, p. 44, which defines it as "pure alcohol removed from any association with water." The use of this concept is all the more justified since Alberta, unlike Quebec and Ontario, bases its markup on the alcohol content of beverages rather than their monetary value.
56. In Ontario as well, nearly 90% of domestic beer is sold by private stores outside the LCBO (see LCBO, *op. cit.*, p. 46, and Statistics Canada, *op. cit.*, p. 23).
57. Vendor Magazine, special edition: "Celebrating the Success of Privatization," 2003.
58. ALCB, *op. cit.*, Appendix.
59. *Ibid.*, p. 57.

The Alberta government would have pocketed many tens of millions of dollars more with the SAQ's sales level than the Quebec government collected from its liquor monopoly.

owned monopoly. Some Quebec critics[60] reproached the Alberta government for not having done this and for thus having sold the branches at an undervalued price. However, the goodwill of branches would hardly be worth very much in buyers' eyes because, unlike a private store in a competitive market, these branches were tightly linked to the ALCB's monopoly position. In fact, many consumers shopped there only because the law prohibited competing stores.

In a competitive context, decisions about where to locate new stores are no longer made by a government monopoly. It is easy to see that a new private store that opens close to what had been a monopoly branch could seriously affect the latter's value. If consumers are truly able to choose, former branches (with their administrative rigidity, artificially high wages, etc.) risk becoming a charge rather than an asset of value to a purchaser. The proof is that, even if broadly undervalued, some of the branches in Alberta did not find buyers during privatization, with merchants preferring to open their own stores. It is hard to see why a merchant would be prepared to buy stores at a higher price (including the alleged goodwill) after declining to do so at an allegedly undervalued price.

Obviously, nothing prevents the Quebec government from trying to gain value for the SAQ's commercial goodwill, but that should not be its priority, and it should not question the privatization process if the value of this goodwill proves in reality to be inexistent. Even if it failed to sell its monopoly's goodwill, it could still rake in $233 million just from selling the SAQ's physical plant, obtaining results similar to Alberta's.[61]

The argument suggesting that the size of the revenues paid to the government justifies the SAQ's existence is thus completely nullified by the facts. Its monopoly is not at all indispensable and, if the SAQ were privatized, the Quebec government not only would pocket the far from negligible sum of more than $230 million in selling its assets but would still be able to continue collecting annual revenues on a similar scale from the private trade in alcoholic beverages.

3.4 Beverage prices

Are prices higher with a privatized system like Alberta's than with monopolies like the SAQ or LCBO?

It is always difficult to compare the prices of products as heterogeneous as alcoholic beverages can be. There may be a substantial difference between two brands of wine, for example, or two vintages of the same wine. Moreover, with prices highly regulated, they will obviously depend on markups and on the various taxes imposed by provincial governments.[62] The difficulty is even greater if the comparison includes Alberta, where there is no single price and where the different stores are free to offer discounts to distinguish themselves from competitors. There exist no official statistical data to tell if the various products are more expensive or cheaper in Alberta compared to the other provinces. However, research conducted by several organizations gives us a general idea.[63] It shows that price levels are quite similar. Depending on the product, Albertans will sometimes pay less and sometimes more than consumers in the other provinces.

— In the year after privatization, the Alberta Liquor Control Board conducted a price survey of products with the highest sales volumes in Alberta, comparing them to prices in Saskatchewan and British Columbia. The survey found that "Alberta private sector retail prices are comparable to the lowest government retail prices available in Alberta's neighbouring provinces." [64]

— Based on a survey of 100 Alberta stores by Westridge Marketing Services,

60. See Poirier and Petit., *op. cit.*, p. 8, where they write: "In the ALCB privatization, it is clear the government sold the buildings without trying to recover the goodwill value of its liquor stores."
61. This had a book value of more than $290 million in 2004-05. See SAQ, *Annual Report* 2005, Consolidated balance sheet, available at *http://www.saq.com/img/ent/rapport05/Etats_financiers.pdf*.
62. For example, the flat markup in Alberta has the effect of making high-end products relatively inexpensive (and low-end products relatively expensive) compared to a markup system such as what exists in Quebec or Ontario.
63. Few price comparisons exist between Quebec, Ontario and Alberta. Most research compares Alberta with its neighbouring provinces.
64. ALCB, *op. cit.*, p. 35.

Table 3 ~ Prices of certain alcoholic products in Canada

PRODUCTS	ALBERTA	QUEBEC	ONTARIO
LABATT BLUE 12 bottles, 5% alcohol	$18.07	$18.97	$19.25
HEINEKEN 6 bottles, 5% alcohol	$9.95	$11.49	$12.35
MOUTON CADET Bordeaux wine, 750 ml, 12% alcohol	$11.76	$15.35	$13.40
LINDEMAN'S BIN 65 Australian wine, 750 ml, 13.4% alcohol	$9.95	$12.45	$10.05
CANADIAN CLUB Whisky, 750 ml, 40% alcohol	$20.95	$21.95	$22.50
ABSOLUT Swedish vodka, 750 ml, 40% alcohol	$21.96	$22.65	$23.00
LAGAVULIN Scotch whisky, aged 16 years, 750 ml, 43% alcohol	$55.89	$76.00	$90.95
REMY MARTIN Cognac, 750 ml, 40% alcohol	$45.96	$54.00	$75.15
TOTAL	$194.49	$232.86	$266.65
	GAP	+19.7%	+37.1%

Source: *Saturday Night*, November 2004, p. 30.

The argument suggesting that the size of the revenues paid to the government justifies the SAQ's existence is thus completely nullified by the facts.

economist Douglas West compared the average price in the province to the average price imposed in 1996 by the British Columbia, Saskatchewan and Ontario boards.[65] Compared to prices in British Columbia, Alberta prices are higher for five product categories (Canadian whisky, vodka, rum, coolers and beer) though cheaper in the five other categories (Scotch whisky, liqueurs, white wine, red wine and other types of wine). But, as the author notes, "It is important to keep in mind, however, that while some average Alberta prices are higher than those in British Columbia, there is substantial retail price dispersion in Alberta. It will frequently be possible for a consumer to find a lower product price in Alberta than in British Columbia provided the consumer shops around."[66]

In comparison with Saskatchewan, the situation is similar: in some categories (Canadian whisky, vodka, rum, white wine and red wine) average prices in Alberta are higher, while in other categories Saskatchewan has higher prices. Compared to Ontario, average prices in Alberta are higher in six categories (Canadian whisky, vodka, rum, white wine, red wine and other types of wine) but lower in the other four categories (Scotch whisky, liqueurs, coolers and beer).

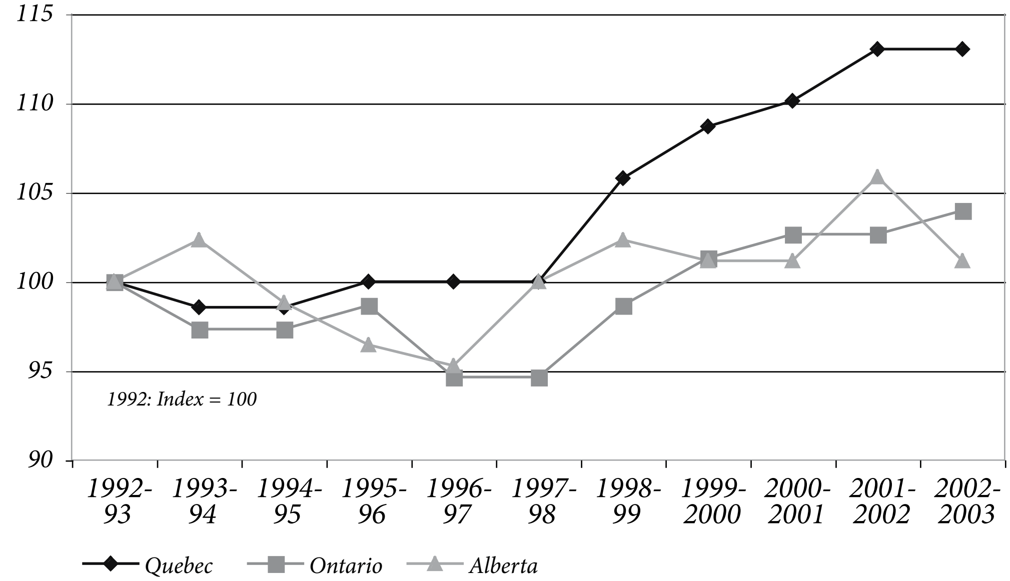
— A 2003 study by the Consumers' Association of Canada covering 53 alcoholic products in British Columbia and Alberta shows that Alberta retail prices may vary considerably (a sign of competition between the various private stores).[67] Although the study does not favour privatization, it observes that for most products the lowest prices that could be found in Alberta were lower than in British Columbia.

— Economist Greg Flanagan, who produced a study critical of privatization of the liquor trade in Alberta, nonetheless concluded that, based on a survey of ten products, "prices, on average, are not dissimilar in the two provinces of Alberta and British Columbia."[68]

— In a survey by the Canadian Taxpayers Federation covering 122 alcoholic beverages, 93% of the products

65. West, *op. cit.*, pp. 54-57.
66. West, *op. cit.*, p. 56.
67. See "Privatization of BC's Retail Liquor Store System," a report by the Consumers' Association of Canada, British Columbia section, May 2003, available at *http://www.consumer.ca/index.php4?id=1542*.
68. Greg Flanagan, *op. cit.*, p. 35.

Figure 5 ~ Change in sales of absolute alcohol per adult 15 years and over, 1993-2003



Source: Statistics Canada, Table 183-0019, "Volume of sales of alcoholic beverages in litres of absolute alcohol and per capita, 15 years and over," fiscal years ending March 31, annual data; calculations by the author.

compared were cheaper in Alberta than in Saskatchewan.[69]

— Finally, a survey published by *Saturday Night* magazine compared the price of a basket of eight products in the various Canadian provinces. The same basket cost nearly 20% more in Quebec, and over 37% more in Ontario, than in Alberta.

All these price comparisons remain incomplete, and the only conclusion we can draw with any certainty based on the available research is that prices in Alberta are generally similar to those in the other provinces and may vary depending on the basket of products. But it is worth emphasizing that Alberta prices could have been made more attractive for consumers if specific regulations had not accompanied privatization and weakened the role played by competition between private stores.

Privatization of the liquor trade in Alberta is not, in fact, complete. The public sector monopoly has been maintained in the areas of wholesaling, storage and distribution (apart from local beer) even though operations have been subcontracted to private enterprise. It is still not possible for someone to open a wholesale business dealing in alcoholic beverages. Similarly, a supplier cannot deliver merchandise directly to a liquor retailer. In any free business, it is sometimes cheaper for a producer or supplier to sell directly to retailers or even to consumers. This is the case, for example, in France, where there is no government monopoly over alcohol and a wine producer can deliver products directly to customers, whether individuals, bars, restaurants or other establishments. The absence of similar competition in Alberta has clearly limited the ability of suppliers and private retailers in Alberta to offer more attractive prices to their customers.

Moreover, the wholesale prices and delivery costs charged to retailers are uniform and regulated. It is impossible to obtain lower wholesale prices based on volume purchases and achieve economies of scale, as is generally the case in other types of truly private business. Stores where transport costs are lower (because they are in less remote areas or easier to reach from the single warehouse in St. Albert) subsidize stores with higher shipping costs. These costs end up being reflected in retail prices.

Also, the new Alberta regulations established in 1993 require liquor stores

69. David MacLean, *op. cit.*, Annexe 1.

to be separate from other types of business.[70] In a truly private market, other retail stores clearly would have been used, with some duties performed by workers who were already hired, with leases already paid, with infrastructure, delivery equipment, storage facilities and so on already provided, thereby avoiding costly investments and keeping prices lower.

3.5 Changes in alcohol sales

Because the number of stores is higher, with new products more readily available to consumers, along with discounts and various other types of promotion, a private system might be expected to stimulate sales and lead to unbridled alcohol consumption. Does this reflect what has happened in Alberta since privatization?

The short answer is no. With private stores in Alberta, almost the same amount of absolute alcohol was being sold per adult in 2003 as in 1993 (close to an average of 8.5 litres per adult per year). Sales rose by only 1.2% during this decade, compared to 13% in Quebec and 4% in Ontario (see Figure 5).

This shows that, even with a government commercial monopoly, alcohol sales can rise far more quickly than with large numbers of private stores.

What ends up emerging from the overall comparison between the performances of the SAQ, the LCBO and the private system in Alberta is that the Alberta system has provided for the creation of a far more dynamic retail trade to the benefit of consumers without per capita alcohol sales running wild. Privatization has provided for increases in the number of stores and in the selection of products at prices that are comparable, all told, to prices found in the other provinces. These changes do not prevent the Alberta government from collecting higher dividends than Quebec and Ontario, in relative terms. The SAQ not only penalizes Quebec consumers but really offers no advantage to the government, which could obtain the same dividends even if it got rid of its liquor monopoly.

The only conclusion we can draw with any certainty based on the available research is that prices in Alberta are generally similar to those in the other provinces.

70. West, *op. cit.*, pp. 23-24 et ALCB, *op. cit.*, p. 9.

Conclusion: Toward a true liberalization

In the 1920s, the Quebec government could boast North America's most liberal and least harmful policy on control of the liquor trade. In 2005, it is among the most restrictive. It seems unprepared to follow the movement toward liberalization and withdrawal from the beverage business, even if all the theoretical arguments and all the facts cry out for doing away with the SAQ's monopoly.

Experience in withdrawal is not lacking in Canada (with the Alberta example) or elsewhere in the world. In Europe, this withdrawal has gone much further than in North America. Most European countries, especially in southern Europe, have no government monopoly over alcohol. And the small number of government monopolies (mostly in the Nordic countries) have in large part been called into question or abolished since the creation of a single market in 1993, when various policies converged toward suppressing controls.[71] Reforms were also accompanied by deregulation. For example, as noted by Esa Österberg and Thomas Karlsson, in most EU member countries "the licensing policy is nowadays a formal procedure where every applicant fulfilling some basic requirements, for instance, of having no criminal record, will obtain [a] licence."[72]

Liberalization of the liquor trade does not necessarily mean that the government no longer plays a role. In European countries, policies governing the liquor trade focus on areas such as controlling advertising and alcohol abuse (for example, driving a motor vehicle while intoxicated). But it is no longer up to the government to monitor and limit consumption, which is each consumer's individual responsibility. Full monopoly systems seem a vestige of the past. According to the authors of the European study, "it seems to be impossible that structures like the comprehensive alcohol monopoly system could be rebuilt in any EU member state."[73]

One scenario suggested by the working group on the alcoholic beverage sector in Quebec in 1997 amounted to a total privatization of the SAQ. The reform was planned in two stages, providing for gradual government withdrawal from the liquor trade. In the first stage, the SAQ would become a private or semi-private company temporarily with the exclusive right to engage in the liquor trade in Quebec (as is currently the case). After this period, "all importing, distribution and retail activities would be fully liberalized."[74]

This type of reform would unquestionably return Quebec to the leading position in North America that it held in the early 20th century. It is time to turn a page that goes back to Prohibition and to conduct a full liberalization of the liquor trade in Quebec.

It is time to turn a page that goes back to Prohibition and to conduct a full liberalization of the liquor trade in Quebec.

71. Esa Österberg et Thomas Karlsson, "Alcohol Policies in the European Comparative Alcohol Study Countries, 1950-2000," Chapter 2, p. 1; available at *http://www.fhi.se/upload/PDF/2004/English/ecas_c_2.pdf*.
72. Ibid., p. 38.
73. Esa Österberg et Thomas Karlsson, "Alcohol Policies in EU States," available at *http://www.ias.org.uk/publications/theglobe/02issue1/globe0201_p12.html*.
74. Working group on the alcoholic beverages sector in Quebec, 1997, *op. cit.*, p. ii. Without going as far as recommending a similar liberalization, an expert committee in Ontario has just suggested ending the LCBO's monopoly and recommended unanimously "that the Ontario government should withdraw from ownership and operation of wholesale and retail" liquor trade (see the report of the Ontario Beverage Alcohol System Review Panel, *op. cit.*, p. 2).

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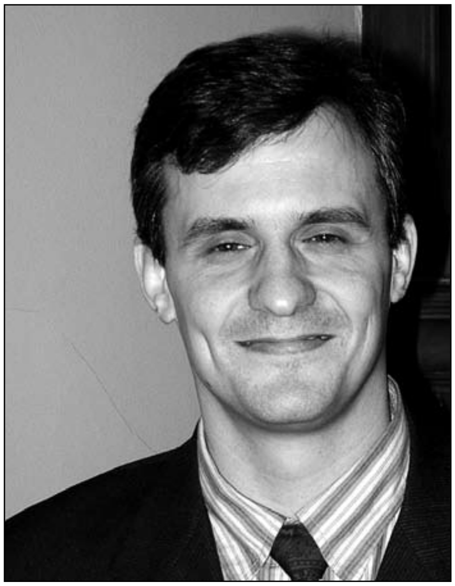

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