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BEER and Small BREW Can Be Good for You

The Federal Beer Excise Tax Is Past Its Shelf Life and Should Be Reformed

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America's beer industry directly supports over 1 million jobs and nearly \$100 billion in economic activity.¹ And over the last two decades, the craft beer market has seen explosive growth. However, the entire beer industry still faces the burden of a specifically targeted excise tax placed on it at the repeal of Prohibition in large part to discourage beer consumption. Today, many politicians, brewers, trade groups, and consumers are seeking relief from the excise tax.² Two competing bills currently pending in Congress, creatively titled the BEER Act and the Small BREW Act, would reduce the tax in different ways. While neither bill is perfect, enacting either one would be a victory for the beer industry and consumers. However, for long-term reform the best course of action is for Congress to repeal the excise tax altogether.

Prohibition's Legacy. In February 1933, with Prohibition winding to a close, teetotaler John Rockefeller, Jr. commissioned a study by Raymond B. Fosdick, an attorney with whom Rockefeller had collaborated on previous studies, and Albert Scott, an engineer friend of Rockefeller's with whom he had worked on a large missionary project, to set forth statutory proposals for states to tightly control and minimize alcohol sales in the post-Prohibition era.³ Adopted in some form by every state, Fosdick and Scott's proposals still largely dominate alcohol policy in the United States. Their study, *Toward Liquor Control*, proposed a high excise tax on alcohol to discourage its use. The federal government enacted such an excise tax just months after Prohibition's repeal. So, while the 14-year Prohibition experiment ended in 1933, this excise tax enacted at the urging of prohibitionists remains with us 80 years later.

Excise taxes on alcoholic beverages have been enacted and adjusted many times throughout our nation's history to raise government revenue, but the post-Prohibition beer excise tax extended beyond that goal to that of influencing individual behavior. Indeed, as Fosdick and Scott saw the tax: "The fundamental objective should be *not revenue but rational and effective social control.*"⁴ Although the Constitution does provide Congress with the "power to lay and collect ...

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excises,”⁵ the constitutionality of a regulation does not necessarily make such a policy wise or just.

The beer excise tax was first levied at \$5 per barrel in 1933. Adjusted several times over the years, the tax was last reset in 1991 to its current rate of \$18 per barrel.⁶ While the original enactment provided no distinction between breweries of different sizes, since 1977, breweries that produce 2 million barrels a year or fewer have been taxed just \$7 a barrel on the first 60,000 barrels and then the full \$18 for each additional barrel produced.⁷ This reduced rate was seen as helping to provide a “pathway to the marketplace” for small brewers.⁸ The excise tax provided roughly \$3.6 billion in revenue to the federal government in 2008.⁹

In addition to the federal excise tax, breweries pay all other taxes levied on businesses, including payroll, income, and state and local taxes. Furthermore, each state imposes its own excise tax on beer ranging from a low of \$0.59 per barrel in Wyoming to a high of \$33.17 in Alaska.¹⁰ On average, half of the cost of a beer is due to federal and state taxes.¹¹ The federal excise tax accounts for roughly 7 percent of the more than \$49 billion in taxes paid each year¹² on \$99 billion in beer sales around the nation.¹³

BEER Act. The Brewers Excise and Economic Relief Act (BEER) Act (H.R. 1918, S. 958), introduced in both chambers of Congress in May 2013, would halve the standard excise tax rate for beer sold in the United States, from \$18 to \$9 per barrel. The majority of the savings will go to macro brewers—multinational breweries producing more than 6 million barrels a year—which account for almost 90 percent of the beer sold in the United States.¹⁴ They do not qualify for the reduced excise tax rates and therefore account for an even greater percentage of the excise taxes paid.¹⁵ But small brewers would also benefit. For small brewers, which it defines as those producing no more than 2 million barrels a year, the BEER Act would eliminate any tax paid on the first 15,000 barrels and would halve the rate on barrels 15,001 through 60,000, to \$3.50. It would keep the qualifying threshold for the reduced rates at 2 million barrels a year.¹⁶ Based on 2012 numbers, the BEER Act would result in tax savings of \$1.68 billion a year.¹⁷

Small BREW Act. The Small Brewer Reinvestment and Expanding Workforce (Small BREW) Act (S. 917, H.R. 494), introduced in the House of Representatives on February 5, 2013 and in the Senate on May 9, 2013, maintains the current \$18 per barrel excise tax rate for beer, but lowers the reduced rate for small brewers even further to \$3.50 per barrel for the first 60,000 barrels produced and to \$16 per barrel for barrels 60,001 through 2 million.¹⁸ It also increases the total number of barrels a brewer can produce in a year and still qualify for these reduced tax rates from 2 million to 6 million. All barrels above the 2 million mark and all barrels produced by brewers who produce more than 6 million barrels will be taxed at the normal rate of \$18. Based on 2012 sales data, the Act will result in tax savings of \$65 million a year, all of which going to brewers producing less than 6 million barrels a year.

Impact. The following table shows the impact the proposed bills will have on brewers of different sizes in terms of total dollars saved, percent reduction in total federal excise tax bills, and the per case savings.¹⁹

Barrels per year	Taxes under current law	BEER Act				Small BREW Act			
		Total	Savings	% Drop	Per Case	Total	Savings	% Drop	Per Case
15,000	\$105,000	\$0	\$105,000	100%	\$0.50	\$52,500	\$52,500	50%	\$0.25
60,000	\$420,000	\$157,500	\$262,500	62.50%	\$0.31	\$210,000	\$210,000	50%	\$0.25
200,000	\$2,940,000	\$1,417,500	\$1,522,500	51.80%	\$0.54	\$2,450,000	\$490,000	16.70%	\$0.18
2,000,000	\$35,340,000	\$17,617,500	\$17,722,500	50.10%	\$0.63	\$31,250,000	\$4,090,000	11.60%	\$0.15
6,000,000	\$108,000,000	\$54,000,000	\$54,000,000	50%	\$0.64	\$103,250,000	\$4,750,000	4.40%	\$0.06
10,000,000	\$180,000,000	\$90,000,000	\$90,000,000	50%	\$0.64	\$180,000,000	\$0	0%	\$0.00

Based on author's calculations

Harvard economist John Friedman has calculated an average per case reduction of \$0.18 under the Small BREW Act. Such a reduction, Friedman estimates, will result in an increased demand of 1.7 million cases of beer from craft brewers and help create 5,230 new jobs in the first year after passage of the Small BREW Act and an additional 400 jobs per year thereafter.²⁰ The assumptions in Friedman's analysis should be viewed with scrutiny. While he assumes that a price reduction of 1 percent will result in an increase in demand for craft beer of 0.88 percent, there is no way to know *how* tax savings would be actually used if either bill is passed. More than 90 percent of the breweries in America produce less than 15,000 barrels a year, meaning they would be receiving less than \$52,000 in savings under the Small BREW Act. They may hire new workers, increase marketing, buy new equipment, or some combination of those activities. There is no similar study looking at the BEER Act, but if Friedman's assumptions are at all accurate, the numbers for the BEER Act will likely be greater given its greater tax reductions.

It is not difficult to see the impact the savings under either bill will have on small businesses in a rapidly expanding industry. For example, Pennsylvania's Victory Brewing Company, at 100,000 barrels and \$18 million in revenue a year,²¹ ranks as the nation's 26th largest craft brewery.²² On October 31, 2012, Victory announced plans to open a new \$50 million brewery that will nearly triple its production capacity, financed by a \$33 million loan.²³ Currently, Victory pays around \$1.14 million a year in federal excise taxes. At its current production level, Victory will save \$622,500 under the BEER Act and \$290,000 under the Small BREW Act. Assuming a 30-year loan repayment plan at 5 percent interest, the BEER Act will provide Victory with roughly a third of its loan repayment money and the Small BREW Act with 15 percent. Upon Victory getting the new brewery running at full capacity, the excise tax reduction under the BEER Act will account for more than the entire repayment of the loan, and that of the Small BREW Act for a third of the repayment. Either bill will make such an expansion significantly more affordable for Victory and many other breweries.²⁴

America's craft brewing industry comprises more than 2,000 small businesses with over 100,000 employees.²⁵ It has experienced a double-digit rate of growth year over year for the last several years.²⁶ As roughly half of the price of a beer is comprised of various federal and state taxes,²⁷ any reduction in the level of taxation on the industry will likely accelerate its expansion.

Brewers must constantly invest to replace and upgrade equipment. A reduction in the excise tax will help all brewers to make those investments, as well as invest in developing new and better products to increase consumer choice and satisfaction. Both of these uses of the money will also create increased economic activity and new jobs.

Concerns about lower prices leading to greater consumption are overblown. The \$0.18 per case reduction calculated by Friedman under the Small BREW Act or the maximum \$0.64 case reduction under the BEER Act are unlikely to result in increased social harms from an increase in alcohol consumption. Friedman's Small BREW Act estimates, which presume the full amount of the tax reduction to be passed through in price savings, only show an increased demand of 1.7 million cases of beer, all coming from craft brewers.²⁸ Considering that Americans drank the equivalent of 2.8 billion cases of beer in 2012, an additional 1.7 million is a relatively small increase when considering potential social harm. Even if the 1.7 million cases were purely new demand—Friedman does not specify whether the increased demand for craft beer will be new or simply a shift from macro to craft beer—the Act will only increase drinking an average of ¼ of a beer per year for each of the 170 million alcohol consumers in the United States.

BEER or Small BREW? Of the two bills, the BEER Act is more beneficial to all brewers, but the industry is divided. There appear to be two primary arguments for the bills: 1) over who will benefit; and 2) over which proposal has a greater likelihood of passage.

The Beer Institute, representing both small and large brewers, supports the BEER Act. The Brewers Association, representing smaller craft brewers, supports the Small BREW Act. Some small brewers are arguing for preserving the status quo, though for different reasons. Lagunitas Brewing Company founder Tony Magee has said he questioned “the basic patriotism of pursuing this roll-back.” Meanwhile, Bell's Brewery founder Larry Bell says he fears that savings to larger breweries will “tip the competitive playing field” in their favor, giving them the opportunity to push the smaller craft brewers out of the market.²⁹

Who Benefits? Brewers are not just concerned with the benefits they will receive from the passage of the BEER Act or Small BREW Act, but with the benefits to their competitors as well. In terms of dollar amounts, most of the savings from the BEER Act will go to the two largest U.S. brewing companies—Anheuser-Busch (now controlled by International conglomerate InBev) and MillerCoors.

Micro brewers' fears that the macro brewers will use any tax savings for increased advertising to push the micro brews out of the market are far-fetched. The large brewers already have significant marketing budgets, so the possible advertising avenues left for the macro brewers to explore are already limited.

Moreover, while even craft beer aficionados become price-sensitive at some pricing level, they would eventually respond to prices only if craft beer hiked their prices significantly, not if macro brewers dropped theirs. And if one of the macro brewers, say Anheuser Busch, were to drop its prices, it would attract mostly consumers of MillerCoors products—unless they adjusted prices in tandem, which would obviously get the attention of antitrust authorities.

Even if the macro brewers were to use tax savings on advertising, craft brewers have been rapidly gaining market share based on quality, despite smaller marketing budgets and higher priced products. While overall beer sales have been declining during the recession, the craft beer industry has experienced double digit rates of growth by offering a product increasing number of consumers consider superior and worth the higher price. No amount of advertising will enable the macro brewers to overcome many consumers' perception of their products as inferior to micro brews.

Ironically, many of the smaller craft brewers have a similar concern about how medium-sized breweries, like Samuel Adams, would use tax savings under the Small BREW Act to further increase their market share and make it harder for smaller craft brewers to increase theirs. Some, like Lagunitas Brewery marketing director Ron Lindenbusch, have speculated that the Small BREW Act is being promoted by the country's largest craft brewery, the Boston Beer Company, which makes Samuel Adams, based on the fact that the Small BREW Act raises the production threshold for who can be considered a small brewer from 2 million barrels to 6 million barrels a year—less than Boston Beer Co.'s annual output.³⁰ But such fears are also unfounded.

Currently, Boston Beer Co. pays the same federal excise tax as the larger breweries. Under the Small BREW Act, Boston Beer Co. will realize savings roughly \$20 million less than under the BEER Act, but it will get a substantial tax cut without its larger competitors also getting a break. It is true that the overall dollar savings from the Small BREW Act's reduced rates for brewers up to 6 million barrels would be greatest for the three breweries that produce between 2 million and 6 million barrels a year: Boston Beer Co; North American Breweries, which sold 2.725 million barrels in 2012; and D.G. Yuengling & Son, which sold 2.79 million in 2012. However, due to Samuel Adams's size and success, its biggest competitors for shelf space and consumers are the macro brewers, not smaller craft brewers. Accordingly, Samuel Adams and the similarly situated Yuengling are the first introduction to a world of beer outside of the macro brews for many consumers—many of whom will branch out and try other craft beer brands, thus benefiting thousands of craft brewers.

As the craft beer industry has rapidly gained market share, macro brewers have become concerned that tax cuts going only to the smaller brewers will accelerate craft beers' growth to the detriment of macro brews. Beer Institute Vice President of Communications Chris Thorne has called the Small BREW Act a "giveaway to a handful of profitable brewers that each are worth more than \$1 billion."³¹ Yet, the growth of craft beers' market share is already under way; a tax reduction on craft brews will only hasten an existing trend. Moreover, a significant portion of beer consumers will likely continue to prefer the taste and cost of macro brews, which will thus retain a significant portion of the beer market.

Likelihood of Passage. Govtrack.us, a government service for tracking legislation pending in Congress, gives the Small BREW Act only a 1 percent chance of becoming law.³² While those are very long odds, they are still better than those for the BEER Act, to which govtrack.us gives a 0 percent chance.³³ However, the Small BREW Act's chances might actually be lower, considering that Greg LaMantia the new Chairman of the National Beer Wholesalers Association, one of the most powerful lobbies in Washington, recently expressed opposition to increasing the small brewer production cap from 2 million to 6 million barrels a year. LaMantia

says that a case could be made for treating an “incubator type brewer” differently, but that “small isn’t 6 million barrels.”³⁴

Moreover, neither bill should be counted out given their substantial numbers of sponsors in both houses of Congress (their low probability of passage from govtrack.us notwithstanding). The BEER Act has 63 sponsors in the House of Representatives and six in Senate. The Small BREW Act has 110 sponsors in the House and 31 in the Senate. Many in the industry, including the Beer Institute’s Chris Thorne, have pointed out that the best chance for either to be enacted into law may be for the whole industry to lend its support to one proposal. Since the largest brewers have nothing to gain from the Small BREW Act, and the BEER Act is more beneficial to all brewers, the latter appears to be the best option for industry-wide support.

On the other hand, in March 2013, Brewers Association CEO Bob Pease told *The Hill* he considers the BEER Act “a defensive measure” designed to “forestall an excise tax increase.” He added, “We certainly do not oppose it. We would favor that bill, but we support our bill, and we are actively working for passage of our legislation.”³⁵ Thus, the Brewers Association prefers the Small BREW Act, which some of its supporters claim has a better chance at passage, because it takes a smaller slice of federal revenue.³⁶

Another concern is that states may see the BEER Act as an opportunity to increase their own excise taxes. While the concern is valid, if speculative, it would still be a better scenario, as it would give the industry a lower across-the-board federal rate, and consumers and brewers would still be able to lobby their state legislatures not to increase taxes on small businesses.

Conclusion. The BEER and Small BREW Acts would benefit America’s beer industry in different ways. While the BEER Act benefits the whole industry and the BREW Act benefits only the craft beer industry, the results of either bill becoming law would be greater profits for businesses and their shareholders, more advertising, business expansion, job growth, and possible lower prices for consumers. Given that both bills face an uphill fight for passage, the industry would be wise to put its whole weight behind just one. Because it benefits the industry as a whole—and benefits all brewers to a greater degree than the Small BREW Act—the BEER Act is the more likely and better option to receive such industry-wide support.

But there is another, better option—full repeal of the federal excise tax on beer, an anachronistic measure designed, and in large part continued, as a means of manipulating consumer behavior. Eliminating the federal excise tax will help produce all of the job creation and business expansion benefits of the BEER and Small BREW Acts to an even greater degree. It will also increase personal freedom by making a significant step toward eliminating controls on alcohol consumption that have dominated the alcohol industry since Prohibition’s repeal.

Notes

¹ *Brewers Almanac*, 2012 economic impact.

² Adam Nason, "Brewers Association formally announces reintroduction of Small BREW Act," *Beerpulse.com*, February 7, 2013, <http://beerpulse.com/2013/02/brewers-association-formally-announces-reintroduction-of-small-brew-act/>.

³ Harry G. Levine, "The Birth of American Alcohol Control: Prohibition, the Power Elite, and the Problem of Lawlessness," *Contemporary Drug Problems*, Spring, 1985: pp. 63-115, <http://dragon.soc.qc.cuny.edu/staff/levine/the-birth-of-american-alcohol-control.pdf>.

⁴ Raymond B. Fosdick & Albert L. Scott, *Toward Liquor Control*, Center for Alcohol Policy, p. 69.

⁵ U.S. Constitution, Art. I, Sec. VIII.

⁶ A barrel equals 31.5 gallons, or approximately 14 cases of 24 12-ounce bottles.

⁷ Internal Revenue Code 5051, <http://www.gpo.gov/fdsys/pkg/USCODE-2011-title26/pdf/USCODE-2011-title26-subtitleE-chap51-subchapA-partI-subpartD-sec5051.pdf>.

⁸ Joe McClain, "Federal excise taxes are beer's most expensive ingredient," *Newark Star-Ledger*, August 28, 2013, http://www.nj.com/times-opinion/index.ssf/2013/08/opinion_federal_excise_taxes_a.html.

⁹ *Brewers Almanac*, History of Federal Excise Tax—Beer (1936 to 2012).

¹⁰ *Brewers Almanac*, History of State Excise Tax Changes.

¹¹ *Brewers Almanac*, 2012 economic impact.

¹² *Ibid.*

¹³ Brewers Association, Beer Sales, 2012 Craft Beer Industry, undated, accessed October 23, 2013, <http://www.brewersassociation.org/pages/business-tools/craft-brewing-statistics/beer-sales>.

¹⁴ The Brewers Association defines craft brewers as those producing no more than 6 million barrels a year and in which an alcohol manufacturer that is not also a craft brewer controls no more than 25 percent.

¹⁵ Brewers Association, Talking Points & Resources: Federal Small Brewer Excise Tax Recalibration Legislation, 2013), accessed October 22, 2013, <http://www.brewersassociation.org/pages/government-affairs/excise-taxes/talking-points-resources>.

¹⁶ As of September 6, 2013, the BEER Act has the support of 63 cosponsors in the House and six in the Senate and has been endorsed by the Beer Institute, a trade organization that represents large macro brewers. It was originally introduced into the House of Representatives on May 2, 2011 and the Senate on May 26, 2011. Despite gaining the support of 123 cosponsors in the House and 9 in the Senate, the bill failed to become law.

¹⁷ Bob Pease message to Brewers Association voting members, Beer Association website, http://brewers.informz.net/Brewers/archives/archive_2341836.html.

¹⁸ As of September 6, 2013, the BREW Act has garnered 110 cosponsors in the House and 31 in the Senate. It has been endorsed by the Brewers Association, a trade group that represents craft brewers. The bill was originally introduced in the House of Representatives on March 29, 2011, where it enjoyed the support of 175 cosponsors, but failed to become law.

¹⁹ A case comprises 24 12-ounce bottles, of which there are 14 per barrel.

²⁰ *Ibid.*

²¹ Joe Satran, "Victory Brewing Company, Veterans In A Field Of Craft Novices, Preps For Expansion," *The Huffington Post*, October 24, 2012, http://www.huffingtonpost.com/2012/10/24/victory-brewing-company_n_2008689.html.

²² "Brewers Association Releases Top 50 Breweries of 2012," Brewers Association press release, April 10, 2012, <http://www.brewersassociation.org/pages/media/press-releases/show?title=brewers-association-releases-top-50-breweries-of-2012>.

²³ "Victory Brewing Company to Expand Operations with Financing from First Niagara," First Niagara, Corporate Communications press release, October 31, 2012, <http://www.victorybeer.com/news/first-niagara-financing/>

²⁴ Authors' calculations.

²⁵ Brewers Association, Talking Points & Resources: Federal Small Brewer Excise Tax Recalibration Legislation, 2013, accessed October 22, 2013, <http://www.brewersassociation.org/pages/government-affairs/excise-taxes/talking-points-resources>.

²⁶ Demeter Group Investment Bank, "State of the Craft Beer Industry," 2013, p. 4, http://www.demetergroup.net/docs/perspective/Craft_Beer.pdf.

²⁷ *Brewers Almanac*, 2012 economic impact.

²⁸ John N. Friedman, Ph.D., “Economic Impact of The Small Brewer Reinvestment and Expanding Workforce Act (H.R. 494)” March 19, 2013,

http://www.brewersassociation.org/attachments/0001/1791/Excise_Tax_Report_Impact-HR_494.pdf.

²⁹ Adam Nason, “Lagunitas reprises opposition re: Small BREW Act, Lindenbusch says Sam Adams behind it,” *Beerpulse.com*, April 11, 2013, <http://beerpulse.com/2013/04/lagunitas-reprises-opposition-re-small-brew-act-lindenbusch-says-sam-adams-behind-it-158/>. Bell says he favors legislation similar to the Small BREW Act that keeps the reduced rates available only to brewers under 2 million barrels, thus ensuring that his brewery receives a tax reduction while his larger competitors do not.

³⁰ *Ibid.*

³¹ Kevin Bogardus, “Beer fight brewing over taxes,” *The Hill*, March 27, 2013, <http://thehill.com/business-a-lobbying/290487-beer-fight-brewing-on-capitol-hill-over-taxes->

³² H.R. 494, Small BREW Act, govtrack.us, <http://www.govtrack.us/congress/bills/113/hr494> Accessed October 23, 2013.

³³ S. 958 BEER Act, govtrack.us, <http://www.govtrack.us/congress/bills/113/s958#overview> Accessed October 23, 2013.

³⁴ “New NBWA Chair Worries about Branches, Sees Opportunities,” Kane’s Beverage Daily, email newsletter, October 2, 2013.

³⁵ Bogardus.

³⁶ Scott Kraus, “Bob Casey taps into beer tax battle,” *Morning Call*, July 15, 2013, http://articles.mcall.com/2013-07-15/news/mc-bob-casey-beer-tax-20130715_1_small-brewers-excise-tax-beer-institute.