House
Legislative
Analysis
Section

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BREWERS' CONSUMPTION/TAX CREDIT

Senate Bill 1064 as passed by the Senate
First Analysis (11-28-00)

Sponsor: Sen. John J. H. Schwarz, M.D.
House Committee: Economic Development
Senate Committee: Economic Development, International Trade and Regulatory Affairs

THE APPARENT PROBLEM:

The Michigan Liquor Control Code regulates the production and sale of beer in the state under what is referred to as the three-tier system. (For more information on the three-tier system, see *Background Information*.) Three types of beer manufacturing licenses are issued by the Michigan Liquor Control Commission: a brewer license (for those who brew over 30,000 barrels a year); a microbrewer license (for those who brew up to 30,000 barrels a year); and a brewpub license (for those who brew up to 5,000 barrels a year and hold a Class C, tavern, or Class A or B hotel liquor license for on-premises sales of alcohol). Brewpubs can sell their own beer for on- or off-premise consumption, but cannot sell directly to wholesalers. Microbrewers can sell their beer for on- or off-premise consumption and can also sell directly to wholesalers, who in turn sell the product to retailers such as stores and bars. Brewers can only sell to wholesalers. In addition, brewpubs and microbrewers receive a tax credit of $2 per barrel from the current tax rate per $6.30 per barrel for beer manufactured or sold in the state.

Intended to help small businesses compete against the larger brewers such as Miller Brewing Company and Anheuser Busch, who reportedly account for 70 percent of beer sales in the nation, the tax credit originally was offered to microbrewers with an annual production of less than 5,000 barrels per year. In 1992, Public Act 300 increased the production limit for eligibility for the tax credit to 20,000 barrels or less per year, and Public Act 440 of 1996 increased the production level to 30,000 barrels or less per year. Therefore, under current licensing restrictions, all brewpubs and microbrewers licensed in the state automatically are eligible to receive the $2 per barrel tax credit. (Out-of-state brewers with a total production level of 30,000 barrels or less per year are also eligible for the credit for beer that is sold within the state.)

In recent years, microbreweries have enjoyed increasing demand for their products. Reportedly, at least one microbrewer in the state is considering opening another brewery. Microbrewers are allowed to have more than one licensed facility in the state, as long as the total production of all the breweries is 30,000 barrels or less per year. Though no microbrewer has yet exceeded the production restriction, it is conceivable that as microbreweries build more plants, or as their products become more popular, they may exceed the annual 30,000 barrel production limit. However, if a microbrewer exceeded 30,000 barrels per year, that business would no longer be considered a microbrewer, but instead a brewer, and the business would also lose the $2 per barrel tax credit. Further, many microbreweries have bars or restaurants attached to the brewery in which their product is sold for both on- and off-premises consumption; once licensed as a brewer, they could no longer sell their beer in these establishments.

Therefore, to continue to encourage small businesses to grow, it has been proposed that the tax credit eligibility be expanded to include brewers whose production level is 50,000 barrels or less per year, but to restrict the credit only to the first 30,000 barrels of production. In addition, it has also been suggested that brewers with an annual production level of 200,000 barrels or less also be allowed to sell their products for on-premise consumption.

THE CONTENT OF THE BILL:

Senate Bill 1064 would add a new section to the Michigan Liquor Control Code (MCL 436.1411) to allow certain brewers that produced under 200,000 barrels of beer per year to sell beer for on-premises consumption. The bill would also revise the current eligibility requirements under which a brewer,

microbrewer, or brewpub may claim a per barrel tax credit (MCL 326.1409).

On-premises Consumption. The bill would specify that a brewer which was not licensed as a microbrewer, but which produced less than 200,000 barrels of beer per calendar year, could sell its beer for on-premises consumption at one location in Michigan that was on any of its licensed brewery premises.

Tax Credit. Currently, under the code, all beer manufactured or sold in the state is taxed at the rate of $6.30 per barrel if sold in bulk or in different quantities. For the purposes of the tax, a barrel of beer contains 31 gallons. An "eligible brewer," defined as a brewer or brewpub that manufactures 30,000 barrels of beer or less during the tax year, may claim a credit of $2.00 per barrel. Senate Bill 1064 would allow an eligible brewer to manufacture up to 50,000 barrels per tax year. However, the bill would retain the $2 per barrel credit only for the first 30,000 barrels produced.

(Note. Currently, the act specifies that a tax of $6.30 per barrel is to be levied on all beer manufactured or sold in the state. That is, on beer manufactured in, or imported into, Michigan. Therefore, it should be noted that the tax credit would also apply to out-of-state brewers that met the bill's production restrictions on beer sold in the state.)

BACKGROUND INFORMATION

The regulatory framework for liquor control in Michigan delineates three separate functions, often referred to as the "three-tier system": manufacturers (distillers and brewers); wholesalers (distributors and suppliers); and retailers (sellers in grocery and party stores, bars, and restaurants). The system was designed to prohibit someone in one tier from having a financial interest in one of the other two tiers. Generally, the laws enacted under the system were devised to prevent vertically integrated monopolies or cartels from participating in the manufacture, distribution, and sale of liquor. In other words, brewers could not own wholesalers or bars, wholesalers could not own breweries or bars, and bars and restaurants could not manufacture or wholesale beer. However, during the past decade, as the beer industry has expanded to include microbreweries and local brewpubs, some feel that the old regulatory framework has been eroded. For instance, Public Act 300 of 1992 provided the opportunity for restaurants to become brewpubs – establishments where beer is both brewed and sold for consumption on the premises. Under Public Act 440 of 1996, brew pubs were allowed to also sell beer off the premises. Further, in 1998, legislation was introduced, but not enacted, that would have allowed a microbrewer to hold a class C license.

FISCAL IMPLICATIONS:

The House Fiscal Agency (HFA) estimates that the bill would have an indeterminate fiscal impact. The bill would allow those brewers who are not licensed as microbrewers, and who produce under 200,000 barrels per year, to sell beer on-premises. This could result in a slight increase in state revenue from sales and income taxes. On the other hand, the bill would allow brewers or brewpubs that manufacture up to 50,000 barrels each year to claim a credit of $2.00 per barrel on the first 30,000 barrels against the tax of $6.30 per barrel. This provision would apply both to beer manufactured in, or imported into, the state, and could result in a slight reduction in state beer tax revenue. (11-14-00)

ARGUMENTS:

For:

A small brewery which prospers to the extent that it manufactures more than 30,000 barrels of beer annually may no longer be defined, under the provisions of the Liquor Control Code, as a "microbrewery." When this happens, the brewery no longer qualifies for the credit of $2.00 per barrel against the $6.30 per barrel tax that would be allowed if its annual production was 30,000 barrels of beer or less. Moreover, the brewery loses its ability to serve beer on the premises at one of its licensed locations. The provisions of Senate Bill 1064 would help such breweries – those whose production is more than 30,000 barrels per year, but less than the production of large breweries, such as Miller or Anheuser Busch. Under the bill, those that produced up to 50,000 barrels per year would still qualify for the tax credit on the first 30,000 barrels they produced. In addition, breweries whose production was less than 200,000 barrels per year would be able to sell beer by the glass at one of their licensed brewery premises. The bill, therefore, would provide important incentives for a business to expand.

Against:

When first established, the $2 per barrel tax credit was designed to encourage small businesses in the brewery field. However, as these breweries have expanded over the years, eligibility for the credit has been extended to encompass the expansion, and some might ask if there is any justification in granting a tax break to a business that has proven its ability to grow. For example, the

credit was introduced under Public Act 130 of 1989 to allow a brewer who manufactured less than 5,000 barrels during a tax year to claim the tax credit. Later, under Public Act 300 of 1992, the tax credit was made available to a brewer manufacturing 20,000 barrels per year. Under Public Act 440 of 1996, the allowable number of barrels was again increased, this time to 30,000. This provision should be deleted.

Against:

Currently, brewers cannot sell beer directly to consumers on their licensed premises (microbrewers and brewpubs *can* sell directly to consumers for both on- and off-premises consumption). Therefore, allowing medium sized brewers to sell their beer to consumers, even if only for on-premises consumption, would constitute yet another attack on the three-tier system. Since the establishment of that system was meant to ensure integrity in the manufacture, distribution, and sale of alcohol, every attempt should be made to preserve it.

POSITIONS:

The Liquor Control Commission (LCC) is neutral on the bill. (11-14-00)

The Michigan Beer and Wine Wholesalers Association is not opposed to the bill. (11-14-00)

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#This analysis was prepared by nonpartisan House staff for use by House members in their deliberations, and does not constitute an official statement of legislative intent.