

K • A • N • S • A • S
WINE & SPIRITS
WHOLESALE ASSOCIATION

February 16, 2017

To: House Committee on Taxation

From: R.E. "Tuck" Duncan, General Counsel

RE: HB2315 — Income tax, rates, modifications, credits; cigarettes and tobacco products, rates; alcoholic beverages, liquor enforcement, rates; business entities, filing fees.



A few weeks ago I distributed to you my recent *Kansas Beverage News* article on beverage alcohol taxation and I refer you to it. The "whiskey tax" is as old as the Republic and was the first tax imposed on a domestic product by the newly formed federal government. Becoming law in 1791 it was intended to generate revenue to reduce the national debt. Now the Governor proposes more beverage alcohol taxes to reduce Kansas' debt. We oppose the increase for the following reasons.

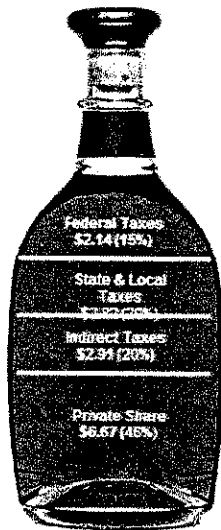
Beverage Alcohol is taxed four (4) times. The federal government collects an excise tax when the product is produced, Kansas collects a gallonage tax when the product comes to rest at a distributor's warehouse, the state collects an 8% tax when the consumer buys a bottle at the liquor store and the consumer pays 10% on the cost of a drink (wine beer or spirits).

The total taxes generated on a \$15.00 liter of spirits =	\$16.26
Federal tax \$13.50 proof gallon /typical 80 proof liter (.264) =	2.85
State Gallonage tax \$2.50 liquid gal, on a liter =	0.66
8% enforcement tax on average \$15.00 liter of spirits =	1.20
10% drink tax on liter (33 drinks @ \$3.50 drink) =	<u>11.55</u>
	\$16.26

Few other products have as many levels of taxation. (over, please)

In the most recent fiscal year FY 2016 Kansas collected \$ 43,792,301 excise (drink) taxes; \$ 67,754,222 enforcement (retail) taxes and \$ 22,192,394 gallonage taxes for a total of \$133,738,917. That was an increase of \$1.1 million or nearly a 1% increase from \$132,589,265 the previous fiscal year's collections. As a general rule liquor taxes have increased in each of the fiscal years this century. Since FY 2011 liquor tax collections have increased by 17 per cent.

***Excessive Tax Burden
Distilled Spirits, 2013***



United States

\$7.87 (54%) Goes to Taxes and Fees

Retail Price of a Typical 750ml Bottle of 80 Proof Spirits: \$14.54

Notes: Indirect taxes include personal income, corporate income, payroll and property taxes. Private Share indicates share received by distillers, importers, wholesalers and retailers.

Beverage alcohol products rank among the highest taxed consumer items available today in the United States.

47% of all Kansas sales are within the 2 counties of the Missouri state line. Folks will cross the border and buy. As a result of doubling the enforcement tax there will be a tax differential between KCMO and Johnson County of 7.65%.

An additional difficulty with increasing taxes on specific products, such as alcohol, is the effect an increase in price has on the demand for the goods.

Economists refer to this as the “elasticity of demand.” If the tax adversely effects price, demand drops and total tax collections are reduced such that the purpose of increasing the tax, more revenue, is defeated.

The budget director concedes we will lose \$95 million in sales at retail (1.5% sales loss at retail for each 1% tax increase), which means a loss of approximately \$75 million at wholesale. In total there is a rollover loss of economic activity (x6) of \$1 billion to the annual Kansas economy.

Alas, in the final analysis, do we really want to raise liquor taxes by \$50 million, and hamper our economy at the cost of 1 billion? One would think not. Please remove the proposed beverage alcohol taxes from HB2315.

Thank you for your attention to and consideration of this matter.

Is Increased Alcohol Taxation on the Horizon?

By R.E. "Tuck" Duncan, Attorney at Law

I write these articles about four weeks before they appear in print. That means that sometimes I have to be clairvoyant. Looking ahead to the Kansas legislative session 2017 my sense is that with the economic woes confronting Kansas government increasing beverage alcohol taxes will be part of the debate. During the past several years sales taxes and cigarette taxes were increased so expecting alcohol taxes to be a subject of discussion doesn't really require me to be psychic. Here are some facts about liquor taxes that you may not know.

The "whiskey tax" is as old as the Republic and was the first tax imposed on a domestic product by the newly formed federal government. It became law in 1791, and was intended to generate revenue to help reduce the national debt. The tax applied to all distilled spirits, but whiskey was by far the most popular distilled beverage in 18th-century United States, so the excise became widely known as a "whiskey tax". The new excise was a part of U.S. treasury secretary Alexander Hamilton's program to pay war debt incurred during the American Revolutionary War. (And to think they made a musical about the guy who taxed whisky. Alas.)

Some of the history of taxation is tied closely to federal regulation. The Trade and Trade Bureau (TTB) reports that:

"The history of taxation and regulatory control on the alcohol and tobacco industries is as old as our nation itself. Since 1789, the United States Treasury Department and its Bureaus have played an integral role in writing its history and in defining our nation's identity. The Department's work with the alcohol and tobacco industries has been carried out by numerous agencies under just as many names. Today, the Department's work with the alcohol and tobacco industries is carried out by the Alcohol and Tobacco Tax and Trade Bureau, or TTB. TTB was created in January of 2003, when the Bureau of Alcohol, Tobacco and Firearms, or ATF, was extensively reorganized under the provisions of the Homeland Security Act of 2002. The Act called for the tax collection functions to remain with the Department of the Treasury, and TTB was born."

"As such, TTB builds upon a rich history, one that is marked with accomplishment and success. After all, it was a Treasury agency that collected the first source of tax income for our new Republic: an excise tax on distilled spirits. These taxes, as called for by Alexander Hamilton, paid off our nation's debt in the Revolutionary War. It was the Treasury Department that found itself in the middle of the Whiskey Rebellion, an event that would later come to stand as the first true test of our Federal government's legitimacy."

"Later, Treasury collected taxes and issued stamps for alcohol and tobacco products in order to finance the Civil War. And during the early part of the twentieth century, the Treasury Department enforced the Eighteenth Amendment, and through the work of agents like Eliot Ness, leader of "The Untouchables," brought to justice those who used the illegal liquor industry to finance organized crime."

A video with an expanded TTB story can be found at: www.ttb.gov/about/story.shtml

With respect to federal taxes the Congressional Research Service, The Library of Congress, issued a report that summarizes present law governing federal taxation of alcoholic beverages and provides a brief history of its development from 1791 to the present. That report notes that:

"Excise taxes on alcoholic beverages began with the 1791 tax, a short lived tax proposed as a means of helping to meet the costs of the Revolutionary War debt. The tax was resurrected briefly during the War of 1812. Eliminated shortly after the close of that war it reappeared as a tool for financing the Civil War, when a tax was also extended to fermented beverages (beer and ales). It has continued through to the present day, being extended to carbonated wines and, just prior to World War I, to wines generally. Taxation of alcoholic beverages are periodically reevaluated by Congress and the subject of congressional inquiries. Taxes generally have increased during war time periods; and during their early years, when demands on the national government were not as great, revenues from these excises contributed a substantial portion of the total budget. Tax rates on alcoholic beverages remained unchanged from the mid-1950s until 1984,

FROM TOPEKA: Is Increased Alcohol Taxation on the Horizon?

when the tax on distilled spirits was increased by \$2 per proof gallon to \$12.50."

"A proof gallon is a gallon which is 50% alcohol. In 1990, in response to demands for added revenues to reduce the budget deficit there was an across the board increase on beverage alcohol tax rates. According to the House committee recommending that increase, these taxes were selected for an increase because they had not been increased for many years so that the effective rate was substantially lower than when adopted and there was considerable evidence of added social costs from consumption of alcoholic beverages. In the latter context the tax increase was viewed as a user fee to aid in bearing the added costs to government and a potential deterrent to excessive consumption."

"Beer is presently taxed at \$18 per 31 gallon barrel; typical table wines (up to 14% alcohol: Chablis, rose, burgundy) are taxed at \$1.07 per gallon; sweeter fortified wines (14 - 21% alcohol: sherry, port, vermouth) are taxed at \$1.57 per wine gallon. Other rates include Champagne and sparkling wines taxed at \$3.40 per wine gallon and artificially carbonated wines taxed at \$3.30 per wine gallon. Distilled spirits are now taxed at the rate of \$13.50 per proof gallon. A proof gallon is one gallon of 100 proof spirits (50% alcohol). Thus the tax on 80 proof spirits would be .8 x \$13.50 or \$10.80 per gallon. In addition alcoholic beverages are subject to state taxes."

Maps of all state tax rates can be found at:

<http://www.businessinsider.com/beer-wine-and-liquor-taxes-in-the-fifty-states-2013-5>

For additional information on this topic see: CRS Report RS20172, Excise Taxes on Alcohol, Tobacco and Gasoline: www.congressionalresearch.com/RL30238/document.php

For the Kansas consumer beverage alcohol is taxed four times. The federal government collects its excise tax when the product is produced, Kansas collects a gallonage tax when the product comes

to rest at a distributor's warehouse, the state collects an 8% tax when the consumer buys a bottle or six-pack at the liquor store and the consumer pays 10% on the cost of a drink (wine, beer or spirits).

The total taxes generated on a \$15.00 liter of spirits, for example, is \$16.26

Federal tax \$13.50 proof gallon / typical 80 proof liter (.264) = **\$2.85**
State Gallonage tax \$2.50 liquid gal, on a liter = **\$0.66**
8% enforcement tax on average \$15.00 liter of spirits = **\$1.20**
10% drink tax on liter (33 drinks @ \$3.50 drink) = **\$11.55**
That's a total of **\$16.62**

Few other products have as many levels of taxation.

In the most recent fiscal year FY 2016 Kansas collected \$43,792,301 excise (drink) taxes; \$67,754,222 enforcement (retail) taxes and \$22,192,394 gallonage taxes for a total of \$133,738,917. That was an increase of \$1.1 million or nearly a 1% increase from \$132,589,265 the previous fiscal year's collections during difficult economic times. As a general rule liquor taxes have increased in each of the fiscal years this century. In the decade from FY2005 when Kansas collected \$90,246,472 in gallonage, enforcement and excise taxes, there has been an increase in collections of 33% without any adjustments in the rates of taxation. Some say that if you leave the industry be, it will generate more for the state as a result.

The Distilled Spirits Council of the United States (DISCUS) has stated that increasing alcohol taxes punishes the entire hospitality industry. DISCUS works closely with suppliers, wholesalers and retailers to oppose all alcohol and hospitality tax increases because they believe responsible consumers of distilled spirits already pay more than their fair share. There is a wide disparity in alcohol tax rates at the state level with spirits being taxed nearly two times higher than table wine and nearly three times higher than beer. In Kansas spirits gallonage tax is \$2.50, wine 30 cents

and beer 16 cents.

DISCUS notes that beverage alcohol products rank among the highest taxed consumer items available today in the United States. In fact, direct alcohol excise and sales taxes levied at the federal, state, and local levels account for more than one-third of the shelf price of many popular brands. The result is that government at all levels earns \$2 from the sale of beer, wine, and spirits for every \$1 earned by producers, wholesalers, and retailers.

In particular, increasing the gallonage tax is the most insidious because it, like the federal tax, is incorporated into the laid-in cost of the product. The Kansas gallonage taxes as compared to Missouri are already higher, except on wine. Spirits: KS \$2.50/gal MO \$2.00. Beer: KS 18 cents, MO 6 cents. Wine: KS 30 cents, MO 42 cents. Since nearly 50% of all Kansas sales are within 50 miles of the Missouri state line, raising gallonage taxes is particularly destructive to the market. Folks will cross the border and buy.

An additional difficulty with increasing taxes on specific products, such as alcohol, is the effect an increase in price has on the demand for the goods. Economists refer to this as the "elasticity of demand." If the tax adversely effects price (as it would in the KS vs. MO scenario), demand drops in KS and total tax collections are reduced such that the purpose of increasing the tax, more revenue, is defeated. People will still be buying beverage alcohol, just not on this side of the state line.

By the time you read this article we will know if the Governor is proposing a tax increase and you will be prepared to discuss the subject with your legislator. If he doesn't propose one, this "physic" is relatively confident someone else will.

In 1789 Benjamin Franklin wrote: "Our new Constitution is now established, and has an appearance that promises permanency; but in this world nothing can be said to be certain, except death and taxes." How right Old Ben was.