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Mr. Brian Pallister
Chairman
House of Commons Standing Committee on Finance
Wellington Building, Room 664
House of Commons
Ottawa, Ontario
K1A 0A6

Dear Mr. Pallister:

We are writing to submit our views and recommendations to the Finance Committee in its pre-budget consultations on "Canada's Place in a Competitive World".

Introduction and Summary

The Brewers Association of Canada (BAC) is the national association representing brewers from coast to coast licensed to operate in Canada. Our 15 member companies (listed below) account for over 97 per cent of domestic beer sales in Canada.

Fort Garry Brewing Company	Nelson Brewing Company Limited
Great Western Brewing Company Ltd.	Northern Breweries Limited
Labatt Breweries of Canada	Pump House Brewery
Lakeport Brewing Corporation	Sleeman Breweries Ltd.
Magnotta Brewery	Storm Brewing in Newfoundland Ltd.
Molson Canada	Tree Brewing / Fireweed Brewing Corp.
Moosehead Breweries Limited	Wellington County Brewery Inc.
Yukon Brewing Company	

Brewers have been operating businesses in Canada for over 350 years and are a major contributor to the Canadian economy. In 2005, the Canadian brewing industry generated 1.2 per cent of the country's Gross Domestic Product (GDP) at almost \$14 billion in total economic activity. Employment for 188,000 Canadians depends either directly or indirectly on the health and viability of the industry as does more than \$4.3 billion in annual tax revenues.

The news release issued by the Finance Committee announcing the pre-budget hearings states that:

"If Canada is to have a meaningful place in the world of the future, then citizens and businesses – and, by extension, the Canadian economy – must prosper".

We agree and support the Committee in its efforts to explore this broader theme as well as its consideration of the specific question it raises:

"What federal tax and/or program spending measures should be implemented in the upcoming budget to ensure that our businesses are competitive?"

Federal Budget 2006

The federal budget of May 2 introduced tax relief for small and medium-sized Canadian breweries in the form of tiered excise reduction based on production volumes. The Finance Minister showed forward thinking in tabling this measure intended to assist with the competitiveness of these smaller operations. He also, at the request of the industry, subsequently expanded the scope of the relief to include all Canadian brewers on their first 75,000 hectolitres of production.

We thank the Minister for his responsiveness. But at the same time, we raise concerns regarding the other budget initiative which increased the rate of excise duty to offset a reduction in GST from 7 to 6 per cent, effective July 1. This change not only denied the Canadian beer consumer tax relief and placed pressure on an industry faced with stagnant growth, but also produced other consequences:

- the price impacts were highest in absolute and relative terms on the lower-priced value product segment, while the price of premium-priced imports actually decreases;
- the re-allocation of taxes from high priced imports to lower priced domestics shifted more of the tax burden to lower income beer consumers and benefited higher income premium import consumers;
- competitive advantage was moved in the direction of foreign producers over Canadian small brewers which occupy the same market niche, undermining the objective of small brewer tax break announced in the budget, and;

- taxation policy which historically has favoured lower alcohol beverages over higher was altered with hard liquor bearing the lowest rate of increase.

Overall the excise increase of July 1:

- singled out and negatively affected the Canadian beer consumer;
- introduced market and competitive distortions;
- impacted the overall health of the Canadian brewing industry.

Negative Impact on Canadian Beer Consumer

As a result of the excise increase, more than 10 million beer consumers were denied the benefits of the GST reduction announced in the federal budget. With the exception of beer, wine, hard liquor and tobacco, other excise carrying products were not singled out for an increase.

With federal and provincial commodity taxes representing on average 51 cents of every dollar spent on beer, Canadian beer consumers already pay the highest beer taxes in the world, with the exception of the Norwegians. Contrasting the Canadian situation, combined federal and state beer taxes in the United States represent about 19 per cent of the final retail price.

Excise is volume based and therefore the same for all beer. As a result, when that same increase is applied across differing brand categories, which vary in base price but are of equal volume, there is a distortion in the final price paid by consumers. The price impacts in absolute and relative terms are highest on the lower priced domestic value brands while the price of premium-priced imports actually decreases. Revenue neutrality only exists somewhat for mid-priced products which may or may not hold a significant share of market in any given region.

For the Canadian consumer, the re-allocation of taxes from higher priced imports to lower priced domestic categories benefits those with higher incomes at the expense of those on lower or fixed incomes who tend to purchase value brands. This outcome is regressive.

The effect of the recent excise increase was accentuated in some regions due to some provinces imposing a provincial tax on alcoholic beverages based on a percentage of their purchase price, which includes excise. The more a province relies on this ad valorem taxation the greater the impact of an excise duty increase. In terms of rate changes announced for July 1, the beer consumers most affected were those in the less prosperous regions (the Maritimes).

Market and Competitive Distortions

Beer, wine and spirits producers compete for a share of market among the drinking population. The three sectors care about their absolute and relative tax burden, absolute and relative prices and the potential for shifts between sectors arising from tax changes.

In general, around the world and within Canada, measures taken with respect to high alcohol content beverages, such as hard liquor, have been more stringent than the lower alcohol content ones. Inter-beverage studies show there are differences in the constituents, use patterns, and physiological and psychological effects, and that each of these beverages may have a different impact on health and social concerns.

Taxation policy, both within Canada and abroad, has tended to acknowledge these important differences and lean in the direction of preferential treatment of lower alcohol beverages. Yet the rate of the recent excise increase for hard liquor was half that for beer and one-quarter that for wine, representing a departure from previous taxation policy.

Impact on Health of the Industry

Change in the tax system is of vital interest to the brewing industry as it directly affects the ability of the industry to compete in the global economy. This is especially true with respect to the excise levy, which is the first of at least four different taxes levied on alcoholic beverages. In addition, there may be private retailer mark-ups on beer in certain jurisdictions and in all markets the on-premise trade levies its own mark-ups to provide for margin. As a result, a change in excise duty has significant implications for all participants in the sale and distribution chain.

The net effect of the excise increase not only deprived the Canadian consumer of a tax reduction, but also came at an increasingly difficult time for the brewing industry. In the 10 years between 1995 and 2005, per capita consumption of beer has decreased on average by 0.8 per cent annually. During the same period, per capita consumption of total alcohol increased on average by less than 1 per cent a year. The stagnation of the total market, and brewing in particular, would suggest a need for tax relief, not increase, both for the Canadian beer consumer and for the sector.

Of all the taxes paid by brewers, the excise levy is the largest tax component. The weight of this tax compounds the problems associated with other taxes that are insensitive to a firm's profits such as capital, payroll and property taxes, all of which have become a larger part of total business taxes over the years. These taxes compete directly for needed capital and have a significant impact on cash flows which are critical to the ability of companies to compete.

Recommendations

As we have already indicated, the excise increase announced in the federal budget was associated with numerous complexities. With another GST reduction anticipated, it is vital that Canadian beer consumers be allowed to enjoy the benefits of a tax reduction along with other Canadians. We recommend therefore that the excise not be increased further. In fact, the government should initiate a process to reduce excise on beer over time. This would help not only Canadians on an individual level, but also encourage growth within the Canadian brewing industry thereby contributing to the national economic growth envisioned by the Finance Committee.

Yours truly,

A handwritten signature in black ink, appearing to read "Hall", with a long, sweeping horizontal flourish extending to the right.