



ALCOHOLIC BEVERAGES RESEARCH EXEMPTIONS

EVALUATION SUMMARY | JANUARY 2022 | 2022-TE1

EXPENDITURE	ENOLOGY RESEARCH EXEMPTION	MALT LIQUORS RESEARCH EXEMPTION
TAX TYPE	Excise	Excise
YEAR ENACTED	2008	2016
REPEAL/EXPIRATION DATE	None	None
REVENUE IMPACT	\$112	\$131
NUMBER OF TAXPAYERS	3	4

KEY CONCLUSION: The exemptions are being used by public institutions of higher education in Colorado to avoid the administrative burden of remitting excise tax for wine and beer manufactured for research and educational purposes.

WHAT DO THESE TAX EXPENDITURES DO?

ENOLOGY RESEARCH EXEMPTION—Exempts wine manufactured by public institutions of higher education for research and educational purposes from excise tax.

MALT LIQUORS RESEARCH EXEMPTION—Exempts beer manufactured by public institutions of higher education for research and teaching purposes from excise tax.

WHAT IS THE PURPOSE OF THESE TAX EXPENDITURES?

Statute and the exemptions' enacting legislation do not state their purpose; therefore, we could not definitively determine the General Assembly's original intent. However, based on our review of legislative history, statutory language, as well as feedback from stakeholders and the Department of Revenue, our evaluation considered these exemptions to have the following potential purpose: to avoid the administrative burden to

public institutions of higher education in Colorado that would be associated with remitting excise tax on wine and beer that is manufactured for research or educational purposes only and is not intended for sale.

WHAT POLICY CONSIDERATIONS DID THE EVALUATION IDENTIFY?

The General Assembly may want to consider establishing statutory purposes and performance measures for the exemptions.



ALCOHOLIC BEVERAGES RESEARCH EXEMPTIONS

EVALUATION RESULTS

WHAT ARE THE TAX EXPENDITURES?

This evaluation covers two similar alcohol excise tax exemptions provided to public institutions of higher education in Colorado that are engaged in the manufacture of wine or beer for research and education purposes: (1) Enology Research Exemption [Section 44-3-106(5), C.R.S.] and (2) Malt Liquors Research Exemption [Section 44-3-106(6), C.R.S.], referred to in this report collectively as the Alcoholic Beverages Research Exemptions.

- **ENOLOGY RESEARCH EXEMPTION**—Exempts from excise tax vinous liquor manufactured by Colorado public institutions of higher education for the purpose of enology (i.e., study of wine and winemaking) research and education. Vinous liquors, as defined in the Colorado Liquor Code [Section 44-3-103(59)(a), C.R.S.], include wine and fortified wines that contain between 1.5 percent and 21 percent alcohol by volume, and are produced by the fermentation of the natural sugar contents of fruits or other agricultural products containing sugar.
- **MALT LIQUORS RESEARCH EXEMPTION**—Exempts from excise tax malt liquors manufactured by Colorado public institutions of higher education for research and teaching purposes. Malt liquors, as defined in the Colorado Liquor Code [Section 44-3-103(30)(a), C.R.S.], include beer and any beverage obtained by the alcoholic fermentation of any infusion of barley, malt, hops, or any other similar product or combination thereof, in water containing not less than 1.5 percent alcohol by volume.

House Bill 08-1359 created the Enology Research Exemption in 2008, and House Bill 16-1042 created the Malt Liquor Research Exemption in 2016. Both of these bills exempted Colorado public institutions of higher education from the entirety of the Colorado Liquor Code [Article 3 of Title 44, C.R.S.], which, in addition to the imposition of excise taxes, provides for the regulation of alcoholic beverages in the state, including licensing requirements. The exemptions have remained substantively unchanged since their enactments.

According to statute [Section 44-3-503(1)(a), C.R.S.], all alcohol “sold, offered for sale, or used” in Colorado is subject to an excise tax, unless specifically exempt. Therefore, although qualifying schools do not typically sell the alcoholic beverages, without the Alcoholic Beverages Research Exemptions, they could be subject to the tax because it is manufactured in Colorado. EXHIBIT 1 provides the state excise tax rates for beer and wine.

EXHIBIT 1. EXCISE TAX RATES BY ALCOHOLIC BEVERAGE TYPE	
Beverage Type	Tax Rate
Beer, malt liquors, fermented malt beverages	\$0.08 per gallon
Wine	\$0.0733 per liter Additional excise tax surcharges apply based on the total volume produced by a licensed winery (\$0.05 for the first 9,000 liters; \$0.03 for between 9,001 and 45,000 liters; \$0.01 for more than 45,000 liters)

SOURCE: Office of the State Auditor analysis of Section 44-3-503, C.R.S.

State institutions of higher education engaged in the manufacture of wine and/or beer for research and education purposes are not required to report their use of these exemptions on any Department of Revenue (Department) form.

WHO ARE THE INTENDED BENEFICIARIES OF THE TAX EXPENDITURES?

Statute does not explicitly state the intended beneficiaries of the Alcoholic Beverages Research Exemptions. Based on the operation of the exemptions, we inferred that the intended beneficiaries are public institutions of higher education in Colorado that are involved in the manufacture and tasting of malt or vinous liquors for research and educational purposes. As of August of 2021, the following Colorado public institutions had alcoholic beverage research or education programs that qualified for the exemptions:

- Colorado State University
- Colorado Mesa University/Western Colorado Community College
- University of Northern Colorado
- Metropolitan State University of Denver
- Front Range Community College.

Additionally, Morgan Community College was in the preliminary stages of developing an enology research program.

WHAT IS THE PURPOSE OF THE TAX EXPENDITURES?

Statute and the enacting legislation for these exemptions do not state their purposes; therefore, we could not definitively determine the General Assembly's original intent. Based on our review of the exemptions' legislative history, the operation of the exemptions, as well as feedback from stakeholders and the Department, we considered the following potential purpose for the Alcoholic Beverages Research Exemptions: to avoid the administrative burden to state institutions of higher education that would be associated with remitting excise tax on wine and beer that is manufactured for research or educational purposes only, and is not intended for sale.

As discussed, the enacting legislation for both exemptions exempted state institutions of higher education from all requirements of the Colorado Liquor Code [Article 3 of Title 44, C.R.S.] and the bill

sponsors indicated that the intent of the bills was to allow public higher education institutions to avoid the administrative costs of complying with alcohol manufacturing licensing requirements for alcohol that is not intended for sale. Additionally, the Alcoholic Beverages Research Exemptions apply only to public institutions of higher education in Colorado, which are exempt from other types of taxes, such as income and sales tax. According to stakeholders, these schools had not been paying the excise tax before the exemptions were enacted. The exemptions appeared to clarify that their tax-exempt status extends to wine and beer that they produce as part of their research and educational mission.

ARE THE TAX EXPENDITURES MEETING THEIR PURPOSE AND WHAT PERFORMANCE MEASURES WERE USED TO MAKE THIS DETERMINATION?

We could not definitively determine if these exemptions are meeting their purpose because no purpose is provided for them in statute or in their enacting legislation. However, we found that the exemptions are likely meeting the potential purpose that we considered for purposes of conducting this evaluation because Colorado public institutions of higher education are not paying excise tax on the wine or beer that they manufacture for research or educational purposes.

Statute does not provide quantifiable performance measures for either of the exemptions. Therefore, we created and applied the following performance measure to determine the extent to which the exemptions are meeting their inferred purpose:

PERFORMANCE MEASURE: To what extent are public institutions of higher education in Colorado that are engaged in beer or wine manufacturing for research, education, or teaching purposes making use of the Alcoholic Beverages Research Exemptions?

RESULT: Through stakeholder feedback, we determined that malt liquors and enology research and education programs at public institutions of higher education in Colorado are using the exemptions.

We received feedback from all five of the schools with these programs that we identified, and none reported remitting any excise tax for the manufacture of beer or wine for research and educational purposes. However, the majority of schools were unaware that their practice of not remitting excise tax for alcohol manufactured for research and educational purposes is codified in statute. Therefore, for some schools, the exemption may serve to bring their existing practice into compliance with the State's excise tax laws. Combined, the five schools reported manufacturing 473 to 1,533 liters of wine and 1,310 to 1,965 gallons of beer per year for educational and research purposes.

WHAT ARE THE ECONOMIC COSTS AND BENEFITS OF THE TAX EXPENDITURES?

We estimate that the Alcoholic Beverages Research Exemptions reduce state revenue by an average of \$243 per year. Specifically, we estimate that the Enology Research Exemption likely results in an average of \$112 of forgone revenue per year, and the Malt Liquors Research Exemption likely results in an average of \$131 of forgone revenue per year. The Department was not able to provide us with data on the amount claimed for the Alcoholic Beverages Research Exemptions. Therefore, we estimated its revenue impact by obtaining estimates of wine and beer production from each alcoholic beverage research program and multiplying the averages of those estimates by the applicable excise tax rates. For wine, we applied the \$0.0733 per liter excise tax rate plus either the \$0.03 or \$0.05 per liter surcharge depending on the average estimated production of the program and how long they have been in existence. We applied the \$0.08 per gallon excise tax rate for beer.

WHAT IMPACT WOULD ELIMINATING THE TAX EXPENDITURES HAVE ON BENEFICIARIES?

If the exemptions were eliminated, Colorado public institutions of higher education that are engaged in the manufacture of wine or beer for teaching or research purposes would have to pay alcohol excise tax

on their product. This would create additional administrative and financial costs for these programs. Specifically, they would be required to file monthly excise tax returns that include the amount of wine or beer manufactured. They would also be responsible for remitting \$0.08 per gallon of beer manufactured and \$0.0733 per liter of wine manufactured, with additional wine excise tax surcharges added dependent on the quantity of wine manufactured. Additionally, as discussed, conversations with stakeholders revealed that a majority of the institutions were not aware that their practice of not remitting excise tax on the wine or beer they produce for research or educational purposes was codified in statute. Thus, if this expenditure were to be repealed, some stakeholders may not be aware of the need to pay excise tax.

ARE THERE SIMILAR TAX EXPENDITURES IN OTHER STATES?

We did not identify any states with similar exemptions that are explicitly provided in their statutes. However, the District of Columbia adopts all federal alcohol excise tax exemptions in its excise tax laws. This, in effect, works in a similar manner to Colorado's Enology Research Exemption for higher education institutions with wine manufacturing operations that are considered experimental wineries by the Alcohol and Tobacco Tax and Trade Bureau [27 CFR 24.77]. Nevada also has an excise tax exemption for "instructional wineries," but these do not include higher education institutions.

ARE THERE OTHER TAX EXPENDITURES OR PROGRAMS WITH A SIMILAR PURPOSE AVAILABLE IN THE STATE?

There are no similar tax expenditures or programs available at the state level in Colorado.

Public and private institutions of higher education in Colorado that are engaged in the manufacture of wine for the purpose of research or education are eligible to register as experimental wineries with the federal Alcohol and Tobacco Tax and Trade Bureau [27 CFR 24.77]. Experimental wineries are permitted to manufacture wine for tasting,

and they are prohibited from selling wine they manufacture. Experimental wineries are exempt from federal excise tax on wine. There are no similar federal regulations for malt liquors manufactured by public or private institutions of higher education.

WHAT DATA CONSTRAINTS IMPACTED OUR ABILITY TO EVALUATE THE TAX EXPENDITURES?

The Department was unable to provide data on the usage of the Alcoholic Beverages Research Exemptions because public institutions of higher education are not required to report the amount of beer or wine they manufacture to the Department. Therefore, we estimated the revenue impact of the exemptions by obtaining estimates of wine and beer production from stakeholders, and multiplying those estimates by the applicable excise tax rates.

If the General Assembly determines that more accurate figures are necessary, it could require the institutions to begin reporting the amount exempted and direct the Department to add additional reporting lines on the relevant forms. This would also necessitate making changes in GenTax, its tax processing and information system, to capture and extract this information, which would require additional resources (see the Tax Expenditures Overview Section of the *Office of the State Auditor's Tax Expenditures Compilation Report* for additional details on the limitations of Department data and the potential costs of addressing the limitations). However, collecting and reporting this information would impose an administrative burden on enology and malt liquors research programs, and, due to the low revenue impact associated with these expenditures, it may not be practical or cost effective for the Department to amend its forms and capture the data in GenTax.

WHAT POLICY CONSIDERATIONS DID THE EVALUATION IDENTIFY?

THE GENERAL ASSEMBLY MAY WANT TO CONSIDER AMENDING STATUTE TO ESTABLISH STATUTORY PURPOSES AND PERFORMANCE MEASURES FOR THE ALCOHOLIC BEVERAGES RESEARCH EXEMPTIONS. As discussed above, statute and enacting legislation do not provide a purpose or quantifiable performance measures for measuring the effectiveness of the Alcoholic Beverages Research Exemptions. Therefore, in order to conduct our evaluation, we considered the following potential purpose for the exemptions: to avoid the administrative burden to state institutions of higher education that would be associated with remitting excise tax on wine and beer that is manufactured for research or educational purposes only, and is not intended for sale. We identified this purpose based on our review of the legislative history for the exemptions' enacting legislation, feedback from stakeholders, and the operation of the exemptions. We also developed a performance measure to assess the extent to which the exemptions are meeting their potential purpose. However, the General Assembly may want to clarify its intent for the exemptions by providing purpose statements and corresponding performance measure(s) in statute. This would eliminate potential uncertainty regarding the exemptions' purposes and allow our office to more definitively assess the extent to which the exemptions are accomplishing their intended goal(s).