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Report to the Joint Committee on  
Taxation, U.S. Congress

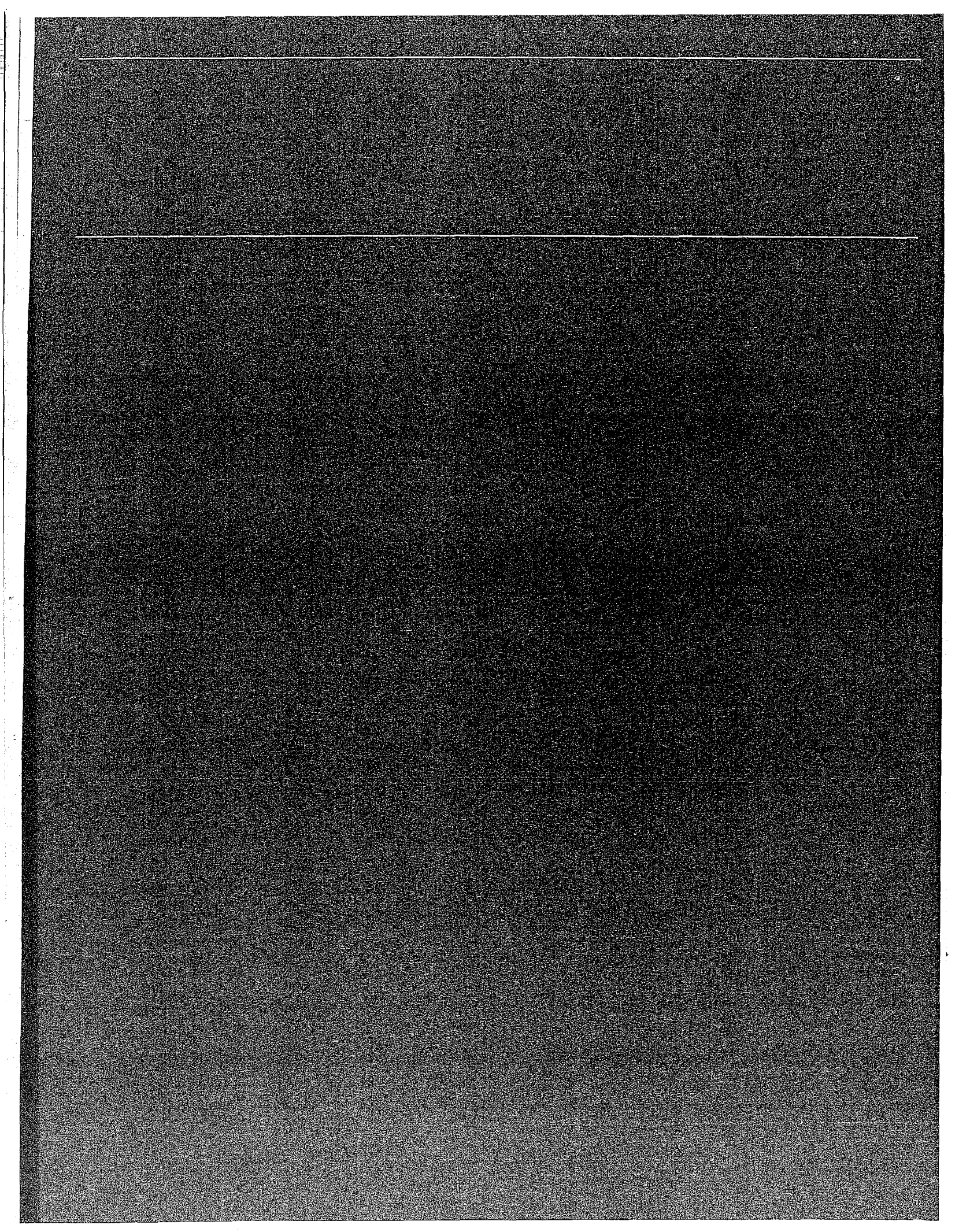
September 1990

# ALCOHOL EXCISE TAXES

## Simplifying Rates Can Enhance Economic and Administrative Efficiency



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General Government Division

B-241041

September 27, 1990

The Honorable Lloyd Bentsen  
Chairman, Joint Committee on Taxation

The Honorable Dan Rostenkowski  
Vice Chairman, Joint Committee on  
Taxation  
Congress of the United States

We have been reviewing the activities of the Bureau of Alcohol, Tobacco and Firearms (BATF). One of our objectives was to examine economic inefficiencies and administrative problems associated with the current alcohol excise tax system. This report documents that information and builds on related information in our prior reports on restoring excise taxes to past levels<sup>1</sup> and improving compliance with occupational taxes.<sup>2</sup> The report was prepared, not at your request, but pursuant to GAO's basic statutory authority. We undertook the effort to assist Congress as it considers possible excise tax changes during the current budget deliberations. A detailed description of our objective, scope, and methodology comprises appendix I.

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## Background

BATF is responsible for collecting the excise taxes imposed on alcohol and tobacco products and certain firearms—taxes that generated a total of over \$10 billion in fiscal year 1989. (See app. II for a list of the excise taxes collected by BATF.) Early excise tax rates were generally established by Congress to generate revenue—especially to meet wartime revenue needs. The current excise tax rates were developed on an ad hoc basis over the years and do not reflect a comprehensive approach considering such factors as economic efficiency and ease of administration.

As discussed in our 1989 report, many excise tax rates are based on per unit amounts rather than a percentage of the product's price and have generally not been changed to account for inflation. Most excise taxes on beer, wine, small cigars, cigarette papers, and some firearms have been imposed at their current rates for almost 40 years or more. Since 1951, for example, inflation has increased prices by about 400 percent. Thus,

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<sup>1</sup>Tax Policy: Revenue Potential of Restoring Excise Taxes to Past Levels (GAO/GGD-89-52, May 9, 1989).

<sup>2</sup>Tax Administration: Compliance and Other Issues Associated With Occupational Excise Taxes (GAO/GGD-86-49, June 5, 1986).

these per unit excise taxes impose a lower tax burden today than when they were last changed. Accordingly, excise taxes have generated a declining percentage of all tax revenues (3.6 percent in fiscal year 1989—down from 8.3 percent in fiscal year 1969). In addition to updating the rates to reflect inflation, some organizations have stated that raising alcohol and tobacco excise taxes could decrease consumption of these products, thereby reducing the associated adverse health effects and other social costs.<sup>3</sup>

The rates for alcohol excise taxes vary considerably by type of product; therefore, beverages with the same alcohol content are taxed at different rates. Distilled spirits are taxed at \$.20 per ounce of alcohol while beer is taxed at \$.05 per ounce and table wine at \$.01 per ounce. Wines with similar alcohol content are also taxed differently, depending on whether they are table wines, artificially carbonated wines (such as wine coolers), or sparkling wines.

Before 1980, all ingredients (including wine, flavors,<sup>4</sup> and distilled spirits) were taxed individually before being combined into a final product. The Distilled Spirits Tax Revision Act of 1979 changed the taxes so they are levied on the final product. To compensate distilled spirits producers who used lower-taxed ingredients (i.e., wine and flavors), Congress amended the Internal Revenue Code (26 U.S.C. 5010) to provide a tax credit. Products such as cordials, liqueurs, blended whiskeys, vodka, and gin are eligible for this tax credit. The credit allows distilled spirits producers to derive up to 50 percent of the alcohol content of their beverage from lower-taxed wine and up to 2.5 percent of the alcohol from lower-taxed flavors, leaving a required minimum of 47.5 percent of the alcohol derived from distilled spirits. Section 5010 reduces the effective tax rate for distilled spirits products containing wine and flavors substantially below the \$12.50 per proof-gallon<sup>5</sup> tax rate for distilled spirits.

In addition to the excise taxes, BATF also administers the special occupational taxes imposed on all businesses that manufacture or sell alcohol,

<sup>3</sup>Federal Taxation of Tobacco, Alcoholic Beverages, and Motor Fuels (Congressional Budget Office, June 1990) and Teenage Smoking: Higher Excise Tax Should Significantly Reduce the Number of Smokers (GAO/HRD-89-119, June 30, 1989).

<sup>4</sup>A flavor is a food additive that is either neutral or can impart both taste and aroma to a beverage but when tasted alone is unfit for use as a beverage.

<sup>5</sup>A proof-gallon is a gallon of 100 proof spirits (50 percent alcohol by volume). The tax on distilled spirits of lower or higher proof is \$12.50 per gallon multiplied by the ratio of the proof to 100.

tobacco, or firearms. Originally established in the 1800s to generate revenue for the Civil War, these taxes generated about \$129 million in fiscal year 1989—primarily from the 420,000 alcohol retailers BATF has identified as liable for the tax. BATF took over responsibility for collecting special occupational taxes from the Internal Revenue Service (IRS) in July 1987, and the Omnibus Budget Reconciliation Act of 1987 increased these rates effective January 1988 (see app. III).

## Results in Brief

Economic inefficiencies and administrative problems have arisen due to the nation's fragmented alcohol excise tax structure. The tax rates were developed on an ad hoc basis without apparent consideration for their collective effect of altering the industry's product development and cost structure or on BATF's administrative burden in implementing these taxes.

The differential tax rates on alcohol products result in similar products being taxed differently. For example, table wine is taxed at a rate 95 percent lower than sparkling wine because the latter was at one time viewed as a "luxury" product. Further, tax differences resulted in a tax credit that has promoted the development of more costly products manufactured to gain the advantage of special tax treatment.

The section 5010 tax credit has provided producers with an incentive to use wine and flavors in distilled spirits products. These additional ingredients can increase the cost of a distilled spirits product by 200 percent or more, but these added costs are more than offset by the tax credit. BATF and industry officials told us that these ingredients are sometimes added to obtain the tax benefits, rather than in response to product requirements, market demand, or cost. Since enactment of the credit, production has outpaced original projections, as have the federal revenue losses, which now total about \$90 million annually. The tax credit also creates administrative problems, and generally BATF is unable to verify compliance with this tax credit without extensive investigation.

We believe that tax rates per ounce of alcohol should be standardized across products to promote more efficient economic decisions by industry and eliminate the need for the credit. Only when taxes are neutral as to product can the market emerge as the primary mechanism governing production decisions. Both consumers and taxpayers could benefit from such a change.

The special occupational taxes BATF administers have become controversial since BATF began identifying and contacting retailers who had been unaware of their obligation to pay the tax. Special occupational taxes are also cumbersome to administer because they require collecting relatively small amounts (\$250 annually for alcohol retailers) from a large number of taxpayers. BATF spent a relatively higher amount of resources to collect special occupational taxes in fiscal year 1989 (\$.08 for every \$1.00 collected) than to collect alcohol and tobacco excise taxes (\$.005 for every \$1.00 collected).

Several options exist for simplifying special occupational taxes. These options would lower both the compliance burdens faced by thousands of small retailers and the administrative burdens faced by BATF. In its fiscal year 1991 budget, the administration has proposed eliminating special occupational taxes on alcohol retailers and increasing special occupational taxes on the lesser number of alcohol producers and wholesalers. An alternative approach, which would eliminate some administrative costs and small business compliance burdens, would be to eliminate the separate occupational tax and slightly increase (by about 2 percent) existing excise taxes on alcohol, tobacco, and firearms to obtain the same amount of revenue. Yet another approach would be to collect alcohol special occupational taxes from only producers and importers (who already file excise tax returns). This could decrease administrative costs while maintaining a special occupational tax.

## Basing Excise Taxes on Alcohol Content Would Equalize the Tax Rates

Excise tax rates on alcoholic beverages were developed on an ad hoc basis over time to generate revenue for various purposes, such as to finance wars, and this process has resulted in different rates for various products. Moreover, the rates of taxation have been eroded due to inflation. For example, as shown in appendix II, most of the current tax rates for beer and wine were last changed in 1951, during the Korean War. The current rates tax beer at about 3.3 percent of the price; it would be about 11.9 percent if it had been indexed since 1951. Table wine is currently taxed at 1.9 percent but would be taxed at 7.1 percent if the rate had kept pace with inflation since 1951.

The excise tax rates for distilled spirits, beer, and wine are not determined by the relative alcohol content of each of these products. Rather, distilled spirits are taxed at \$12.50 per proof-gallon; beer is taxed at \$7



to \$9 per barrel;<sup>6</sup> and wine is taxed at \$.17 to \$3.40 per wine-gallon.<sup>7</sup> Because distilled spirits are taxed more heavily, they provided 66 percent of the alcohol excise tax revenues in fiscal year 1989.

When comparing these tax rates on the basis of an ounce of alcohol, distilled spirits are taxed at the rate of \$.20 per ounce, beer is taxed at \$.05 an ounce; and table wine (with less than 14 percent alcohol) is taxed at \$.01 an ounce. Taxing the alcohol content in all these beverages equally would eliminate the current mix of different rates that depend on factors such as the type of product or the ingredients used. For example, some wines actually derive most (about 90 percent) of their alcohol content from adding distilled spirits to a fermented wine (these are fortified wines). Yet because the final product is classified as a wine, it is taxed at a lower rate, although most of the alcohol it contains is derived from distilled spirits.

There are also some significant differences in the current tax rates that result in disparate treatment of similar products and therefore affect consumers of these products. For example, a table wine that sells for \$25 a bottle is taxed at \$0.17 a wine-gallon while a sparkling wine that sells for the same or a lower price and contains the same amount of alcohol is taxed at \$3.40 a wine-gallon. The tax on sparkling wine has been viewed as a luxury tax. In today's market, however, premium table wines can cost as much or more than sparkling wines, but they are taxed at a rate that is 95 percent lower.

## Different Alcohol Tax Rates Encourage Production Inefficiencies

The differences in tax rates on various alcohol products prompted Congress to amend the Internal Revenue Code in December 1980 to provide a tax credit for producers who use wine or alcoholic flavors in their distilled spirits products. It was designed to offset the effect of the differential tax rates by compensating distilled spirits producers who used lower-tax ingredients (wine and flavors) in their products. This tax credit, which producers claim on their excise tax returns, can lower the effective tax rate for a distilled spirits product from the current rate of \$12.50 per proof-gallon to as low as \$6.30 per proof-gallon.

The section 5010 tax credit acts as an incentive to use wine and flavors in distilled spirits products to achieve a lower tax rate. The addition of

<sup>6</sup>One barrel contains 31 gallons.

<sup>7</sup>A wine-gallon is a phrase used by BATF to distinguish it from a proof-gallon. It is equivalent to one gallon of wine.

wine and flavors may comprise up to 52.5 percent of the alcohol content of the beverage—50 percent from wine and 2.5 percent from flavors. These additives can be used in a wide variety of distilled spirits beverages, such as cordials, pre-mixed cocktails, blended whiskeys, gin, and vodka, without substantially changing the beverages' character or taste.

BATF and private industry officials said that some distilled spirits manufacturers have changed their production processes to qualify for this credit. Producers of some commonly used fruit wines said that adding their wines to distilled spirits products doubles the manufacturing costs because the wine additives cost more than distilled spirits. Table 1 shows an example BATF provided that illustrates how the tax credit lowers the total production cost (including taxes). A 42-proof cordial's material costs would increase from \$.27 (using only distilled spirits) to \$.81 per gallon when using the maximum amount of wine allowed—50-percent wine content. At the same time, the tax credit would reduce the tax expense by \$2.28, thereby lowering the cordial's total cost by \$1.74 per gallon.

**Table 1: Comparative Costs Per Gallon of a 42-Proof Cordial Containing Various Levels of Wine**

	Distilled spirits	25 percent wine	50 percent wine
Cost of spirits	\$.27	\$.20	\$.13
Cost of wine	.00	.34	.68
Total cost of materials	.27	.54	.81
Tax expense	5.25	4.11	2.97
Total cost per gallon	5.52	4.65	3.78
Net cost advantage <sup>a</sup>	.00	.87	1.74

<sup>a</sup>Net cost advantage is the overall cost difference between using only distilled spirits in a cordial and adding wine ingredients. It is the sum of the additional material costs and the amount of tax savings.

Source: Bureau of Alcohol, Tobacco and Firearms.

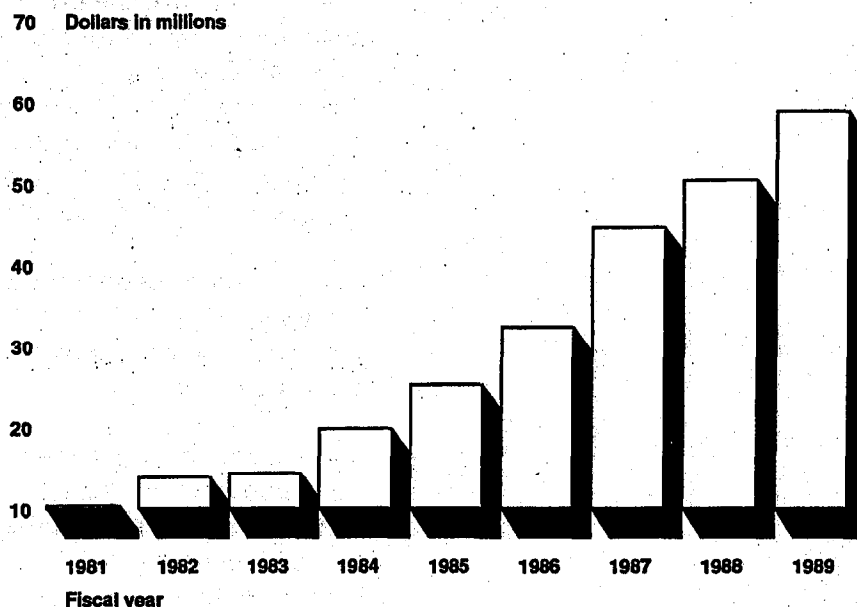
We believe that this incentive provided by the tax credit distorts the production process because it encourages an inefficient allocation of resources to make these products. Taxing the ingredients differently leads to an inefficient combination of ingredients because production decisions are based on tax rates, not on which ingredients are less costly.

In addition to increasing economic inefficiency, significantly more tax revenues are being lost through use of this tax credit than Congress originally estimated. When the credit was enacted in 1980, Congress estimated that the total credits for both domestic and imported products



would be about \$19 million annually (or about \$28 million annually in 1989 dollars). Use of the credit has increased steadily, however, and BATF's data show that in fiscal year 1989 the credit amounted to about \$90 million—\$60 million for domestic and \$30 million for imported products. Figure 1 shows the increase in tax credits taken by domestic manufacturers during fiscal years 1981 through 1989.

**Figure 1: Domestic Tax Credits Taken Under Section 5010**



Source: BATF estimates.

### The Section 5010 Tax Credit Causes Administrative Problems

In addition to the revenue loss and economic inefficiencies due to the credit, BATF also has some problems administering section 5010. Because it would be cheaper for manufacturers to use distilled spirits and a trace of wine or flavors and then claim the credit without actually using the lower-taxed wine and flavors, it is important that BATF ensure compliance with the provisions of the credit. BATF attempts to monitor the use of this tax credit by verifying that the wine and flavors were in fact added to the beverage for the tax credit, but BATF officials told us that BATF is unable to adequately ensure full compliance with this credit for several reasons.

First, laboratory tests, while sufficiently detailed to examine parts per billion of each ingredient, cannot determine the source of the alcohol

contained in the beverage. Therefore, a thorough inspection of the company's records is required to determine exactly what ingredients were used to make the product.

Second, inspecting the records of companies claiming this tax credit can be relatively complex and time-consuming in comparison with other alcohol inspections because the inspectors must trace the sources of all alcohol used in each beverage. Distilled spirits plants may produce several different beverages, each taxed at different effective rates, and may also change the products' formulas. A BATF official said that it is difficult for inspectors to determine whether the correct amount of tax was paid in each instance. When claiming the tax credit, all credits from the company's various products are totalled into one line item, so it is not clear from the tax return specifically for which products the credit is being claimed and how much is being claimed for each product. Verifying the amount claimed requires checking the supporting records.

Third, inspectors do not have the authority to inspect distilled spirits plants in other countries. As a result, BATF is unable to verify that wine or flavors have actually been added to imported products that claim the tax credit.

The section 5010 tax credit has made using costly wine additives a viable option for distilled spirits producers, but for BATF it is both difficult to administer and enforce. The resources used to produce products to meet demand generated by this tax credit could be more efficiently used elsewhere in the economy. Taxing an alcoholic beverage on the basis of its alcohol content, rather than on how it was made, would be a more efficient approach. Such an approach would eliminate any need for this tax credit, thus simplifying both the tax system and its administration.

## The Current Structure for Collecting Alcohol Special Occupational Taxes Is Inefficient

Special occupational taxes on alcohol, tobacco, and firearms businesses provide a relatively small amount of revenue, although the taxes were originally enacted to generate revenue. Of the almost \$129 million generated by these taxes in fiscal year 1989, \$127 million came from alcohol taxes, \$1.6 million from firearms taxes, and about \$.2 million from tobacco taxes.<sup>8</sup> Special occupational tax rates range from \$250 for alcohol retailers to \$1,000 for manufacturers and other businesses, as shown in appendix III.

<sup>8</sup>Numbers do not add to \$129 million due to rounding.

Most of the special occupational taxes BATF collected (almost \$118 million, or about 91 percent of the total) are from alcohol retailers. According to a BATF official, BATF has identified about 420,000 of the 550,000 estimated retailers liable for paying special occupational taxes. The lists of eligible taxpayers must be continually updated as companies start or go out of business. Alcohol retailers subject to the current special occupational taxes range from high volume liquor stores to small "mom and pop" grocery stores. Other businesses that sell alcohol (such as private clubs, limousines with a bar or that serve champagne, and florists that deliver wine and flowers) are also liable for the special occupational tax.

Since assuming responsibility for special occupational tax collections from IRS in July 1987, BATF has had problems identifying all of the alcohol retailers subject to the tax and collecting amounts due from them. When BATF took over responsibility for these taxes, it matched information from IRS' database with state liquor license lists to identify those who were not paying the tax.<sup>9</sup> Some of the noncompliant retailers BATF identified were not aware of the tax and, because they had not paid for many years, owed substantial sums (including penalties and interest). This resulted in numerous complaints to Congress from affected retailers.

These special occupational taxes are relatively costly to administer, particularly when considering the small amount of revenue generated. BATF estimated that it spent \$10.3 million to collect the \$129 million in special occupational taxes in fiscal year 1989—a cost of \$.08 for every \$1.00 collected. In contrast, alcohol and tobacco excise tax collections amounted to \$10.1 billion in fiscal year 1989, and BATF estimates it cost about \$51.5 million to collect—a cost of \$.005 for every \$1.00 collected, which was about 16 times lower than the collection cost for special occupational taxes.

## Alternative Approaches Could Improve Special Occupational Tax Collections

In its fiscal year 1991 budget, the administration has proposed eliminating the special occupational tax on retail alcohol dealers and increasing the special occupational tax rates for the 11,000 wholesalers and 2,100 alcohol producers. By reducing the number of taxpayers, the administration expects that compliance will improve and that the tax will cost less to administer. This proposal, which would involve flat

<sup>9</sup>Tax Administration: Compliance and Other Issues Associated With Occupational Excise Taxes (GAO/GGD-86-49, June 5, 1986), page 30.

amounts applied to wholesalers and producers, was designed to generate at least \$190 million annually—\$61 million more than was collected under the current rate structure in fiscal year 1989.<sup>10</sup>

The administration's proposal to eliminate special occupational taxes on retailers would significantly increase the tax burden for wholesalers and producers, who paid approximately \$7 million of the \$129 million collected in fiscal year 1989. Their increased tax liability would be substantial (from the current rates of \$500 or \$1,000 to new rates of \$12,000 for wholesalers and either \$30,000 or \$65,000 for each manufacturing facility). This tax structure would have taxpayers with vastly dissimilar incomes paying the same higher amount.

Industry representatives and BATF said these increases could adversely affect small producers who would be unable to pay the increased tax. Small producers would probably be unable to pass this higher tax on to consumers because they have to price their products competitively in the market. Large producers, on the other hand, could recoup some of the additional cost by increasing prices by only a small amount. The industry representatives also question the fairness of taxing compliant taxpayers (producers and wholesalers are issued permits by BATF and thus are easily identified) more heavily because others (alcohol retailers) are not compliant.

Fairness, including the ability to pay, is important to consider in restructuring special occupational tax rates. In addition, the purpose of the tax should be considered. If special occupational taxes are levied primarily to obtain revenue (as when they were first enacted), we believe that a better alternative would be to eliminate special occupational taxes altogether and increase the excise tax rates sufficiently to offset the decrease in occupational tax receipts. Given the current amount of alcohol, tobacco, and firearms excise taxes BATF collects (over \$10 billion in fiscal year 1989), the adjustment required to obtain the \$190 million that the administration is proposing would be minimal. Existing excise tax rates would have to be increased by about 2 percent to generate this amount of revenue. This approach would be more efficient and less costly than maintaining separate accounting and collection efforts for special occupational taxes.

<sup>10</sup>Another alternative the administration is considering is to require wholesalers to verify that retailers have paid their special occupational taxes before allowing them to purchase any alcoholic beverages. According to BATF officials, this system would be similar to procedures wholesalers now follow for state liquor licenses and could generate additional revenue by increasing compliance without changing the existing tax structure.

On the other hand, if Congress now intends special occupational taxes to act as a user fee to recoup some of the costs associated with regulating these industries, then Congress may not want to eliminate them. An alternative approach would be to tax alcohol producers and importers and vary the special occupational tax due on the basis of the size of the company. Although this approach differs from the administration's proposal in that it would not tax wholesalers, it is similar in that it would eliminate the special occupational tax for retailers and would, therefore, be more efficient and easier for BATF to administer. By not taxing wholesalers, this approach eliminates the need for a separate collection mechanism for wholesalers since they do not pay alcohol excise taxes. In addition, producers and importers are the primary "users" of BATF's regulatory activities. As part of this approach, Congress could vary the taxes by establishing several categories on the basis of the size of the company so that large producers and importers would pay a proportionally larger share of the tax.

## Conclusions

The existing structure of the alcohol excise tax system has led to economic inefficiencies and administrative problems. Standardizing the tax rates on the basis of the alcohol contained in the product, rather than on the basis of what ingredients it contains, would encourage more efficient economic decisions by producers and eliminate the need for the section 5010 tax credit.

The special occupational taxes, now primarily paid by alcohol retailers, are both difficult to collect and administer. The same amount of revenue could be generated and special occupational taxes could be eliminated altogether by slightly increasing existing excise taxes on alcohol, tobacco, and firearms. If Congress does not want to eliminate special occupational taxes entirely, collecting them only from alcohol producers and importers and varying the tax on the basis of the size of the facility could reduce administration and collection costs.

In addition, the excise taxes BATF administers have not been changed for years, and they impose a lower tax burden than when they were last changed. Indexing these taxes or converting them to rates that represent a percentage of the price of the product would help them keep pace with inflation.

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## Matters for Congressional Consideration

In our opinion, due to the economic inefficiencies and administrative burdens existing under the current excise tax rate structure, Congress should consider simplifying the structure of alcohol excise taxes. First, Congress should consider standardizing alcohol excise tax rates across products on the basis of the percentage of alcohol in a beverage regardless of the mix of ingredients, thereby permitting the elimination of the section 5010 tax credit.

Congress should also consider the role of special occupational taxes in relation to the broader excise tax rate structure. Given the excessive administrative costs and compliance burdens involved in generating relatively small amounts of revenue, Congress should consider changing the special occupational tax by either (1) eliminating it with a corresponding increase in excise tax rates or (2) collecting the tax from only producers and importers and varying the tax on the basis of the size of the facility.

As Congress deliberates about the structure of these taxes, it may also want to adjust the rates to keep pace with inflation as we pointed out in our 1989 report on excise taxes.

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BATF officials reviewed a draft of this report. They agreed that we accurately presented the information contained in this report, especially the information on the difficulties of administering the section 5010 tax credit and the various alternatives for restructuring the special occupational tax. They also provided additional information that we incorporated into this report.

We are providing copies of this report to the House Ways and Means Committee, the Senate Finance Committee, the Director of BATF, and the Secretary of the Treasury. Copies will be made available to other interested parties upon request.



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The major contributors to this report are listed in appendix V. If you have any questions, please contact me on 272-7904.

*for Jennie S. Stathis*  
Paul L. Posner  
Associate Director, Tax Policy  
and Administration Issues

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**Contents**

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**Abbreviations**

BATF      Bureau of Alcohol, Tobacco and Firearms  
IRS        Internal Revenue Service

# Objective, Scope, and Methodology

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Our objective was to identify economic inefficiencies and administrative problems relating to excise taxes administered by BATF that may be of interest to Congress as it considers changes to those taxes. Specifically, our review covered the structure of alcohol excise tax rates, the use of the section 5010 tax credit, and the administration of special occupational taxes.

We based our analysis on information obtained from BATF regarding excise tax revenues, collection processes, and other issues concerning the section 5010 tax credit and special occupational tax collections. We interviewed BATF officials and obtained budget, accounting, and staffing data at BATF's Tax Processing Center in Cincinnati, Ohio, which is primarily responsible for special occupational tax collections. We reviewed the June 1990 Congressional Budget Office study on the "Federal Taxation of Tobacco, Alcoholic Beverages, and Motor Fuels" as well as prior GAO reports and various articles on excise taxes and excise tax policy. We met with representatives of the alcohol industry to discuss their views on alcohol excise tax credits and special occupational taxes. We also reviewed the legislative history of current excise and special occupational tax rates as well as the tax credit provided by section 5010.

We did our work from December 1989 to July 1990 in accordance with generally accepted government auditing standards.

# Selected Excise Taxes, Their Current Rates, and Effective Year of Last Change

Type of tax	Current rate	Effective year of last change
<b>Alcohol</b>		
Distilled spirits	\$12.50/proof gal.	1985
Wines with more than 24 percent alcohol	\$12.50/proof gal.	1985
<b>Wines</b>		
Less than 14 percent alcohol	\$0.17/wine gal.	1951
14 percent to 21 percent alcohol	\$0.67/wine gal.	1951
21 percent to 24 percent alcohol	\$2.25/wine gal.	1951
Artificially carbonated wines	\$2.40/wine gal.	1951
Champagne and other sparkling wines	\$3.40/wine gal.	1951
<b>Beer</b>		
Large brewers	\$9/barrel	1951
Small brewers	\$7/barrel	1977
<b>Tobacco</b>		
<b>Cigars</b>		
Small	\$0.75/1,000 cigars	1926
Large	8.5 percent of wholesale price, not to exceed \$20/1,000 cigars <sup>a</sup>	1977
<b>Cigarettes</b>		
Small	\$8/1,000 cigarettes	1983
Large	\$16.80/1,000 <sup>b</sup>	1983
Cigarette papers	\$0.005/50 papers <sup>c</sup>	1917
Cigarette tubes	\$0.01/50 tubes <sup>c</sup>	1917
<b>Smokeless tobacco</b>		
Snuff	\$0.24/lb.	1986
Chewing tobacco	\$0.08/lb.	1986
Pipe tobacco	\$0.45/lb.	1989

(continued)

**Appendix II  
Selected Excise Taxes, Their Current Rates,  
and Effective Year of Last Change**

Type of tax	Current rate	Effective year of last change
<b>Firearms<sup>d</sup></b>		
<b>Transfer taxes</b>		
Weapons in general <sup>e</sup>	\$200/firearm/transfer	1934
Any other weapon <sup>f</sup>	\$5/firearm/transfer	1960
Making fees	\$200/firearm	1952

<sup>a</sup>The \$20 ceiling on large cigars was established in 1942.

<sup>b</sup>Large cigarettes measuring more than 6 and 1/2 inches in length are taxed at the rate prescribed for small cigarettes, counting each 2 and 3/4 inches (or fraction) as one cigarette.

<sup>c</sup>Cigarette papers and tubes measuring more than 6 and 1/2 inches in length are taxed at \$.005/50 and \$.01/50 respectively, counting each 2 and 3/4 inches (or fraction) as one paper or tube. Tax does not apply to a book or set of cigarette papers containing 25 or fewer papers.

<sup>d</sup>Refers solely to National Firearms Act taxes currently administered by BATF. Regular firearms and ammunition are taxed at a percentage of the sales price.

<sup>e</sup>Includes certain dangerous weapons, such as machine guns, silencers, and destructive devices.

<sup>f</sup>The term "any other weapon" is statutorily defined and includes sporting rifles, fountain pen guns, belt buckle guns, and cane guns.

Source: Joint Committee on Taxation and relevant legislation.



# Special Occupational Tax Rates

Type of business	Annual rate
<b>Alcohol</b>	
Retail dealers (distilled spirits, wine, or beer)	\$250
Wholesale dealers (distilled spirits, wine, or beer)	\$500
Brewers	\$1,000 <sup>a</sup>
Nonbeverage drawback claimant	\$500
User/dealer of industrial alcohol	\$250
Alcohol fuel plant	\$1,000 <sup>a</sup>
Distilled spirits plant	\$1,000 <sup>a</sup>
Bonded wine cellar, warehouse, or bottling house	\$1,000 <sup>a</sup>
<b>Tobacco</b>	
Manufacturer of tobacco products	\$1,000 <sup>a</sup>
Manufacturer of cigarette papers and tubes	\$1,000 <sup>a</sup>
Tobacco export warehouse	\$1,000 <sup>a</sup>
<b>Firearms</b>	
Firearms importer	\$1,000 <sup>a</sup>
Firearms manufacturer	\$1,000 <sup>a</sup>
Firearms dealer	\$500

<sup>a</sup>These taxpayers are eligible for reduced rates (\$500 rather than \$1,000) if their total gross receipts for the most recent income tax year (not just receipts relating to the activity subject to special occupational tax) are less than \$500,000.

Note: The Omnibus Budget Reconciliation Act of 1987 increased the special occupational tax rates. Before January 1988, retail alcohol dealers who sold beer only were taxed at \$24 a year, and retailers selling wine or liquor were taxed at \$54 a year. These rates are now \$250 annually. The top special occupational tax rate was increased from \$500 to \$1,000.

# Summary of GAO's May 1989 Report on the Revenue Potential of Restoring Excise Taxes to Past Levels

We examined per unit excise taxes imposed on alcohol, tobacco, gas guzzler cars, certain weapons, and wagering occupations. Had the excise taxes covered in our review been indexed to keep pace with inflation, the Joint Committee on Taxation estimated that they would have generated additional revenues of \$2 to \$13 billion in 1989 and \$12 to \$75 billion over the 5-year period from 1989 to 1993. (See table IV.1.) The estimates vary depending on the index used and the time period indexed.

Besides indexing, another option for maintaining the real dollar value of excise tax rates in the future is to convert per unit rates to rates that represent a percentage of the price of the product (i.e., ad valorem rates). These ad valorem rates could be set to produce the same revenues as the indexed per unit rates.

Beyond the revenue considerations involved in a decision to maintain excise tax rates in real dollar terms, tough tax policy issues are involved. Both proponents and opponents of rate increases strongly argue their positions. In addition, administrative difficulties may be encountered if rates are indexed or changed to an ad valorem structure. We do not believe these difficulties are insurmountable.

**Table IV.1: Lowest and Highest Revenue Estimates for 1989 for Indexed Excise Taxes**

Dollars in millions

Excise tax group	Current rates	Indexing since date of last change		Indexing since 1965	
		Lowest	Highest	Lowest	Highest
Alcohol	\$4,292	\$5,604	\$8,005	\$7,787	\$10,807
Tobacco	3,342	3,608	5,299	5,449	9,868
Gas guzzlers	65	69	71	69	71
Weapons	2	5	7	2	2
Wagering occupations	8	9	11	21	28
<b>Total<sup>a</sup></b>	<b>\$7,708</b>	<b>\$9,296</b>	<b>\$13,393</b>	<b>\$13,328</b>	<b>\$20,776</b>

<sup>a</sup>Totals may not add due to rounding.

Note: Figures are the lowest and highest dollar values estimated for the tax regardless of the type of index used or the date of last change.

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