

February 26, 2013

Government of Alberta
408 Legislature Building
Edmonton, Alberta, T5K 2B6

Attn: Hon. Thomas Lukaszuk, Deputy Premier

Dear Minister Lukaszuk:

RE: Follow up to our letter dated August 27th 2012 (attached) regarding the Province's Graduated Mark-Up System

We are writing in follow up to the above noted letter sent August 27, 2012, which we have attached for your reference.

Alberta's small brewers still strongly support all of the proposals outlined in our previous letter, some of which we will reiterate here together with some new important facts about Craft Breweries and beer consumption in this province. They are as follows:

- 1) The Alberta beer industry needs a 'Made in Alberta' beer policy.

In an ideal world, where every Province provided brewers with a graduated mark-up program and had free, open and fair access to retail shelves, we would support applying the graduated mark-up program to all. But that is not the case as the market in Alberta is structurally unique on the Canadian landscape. Retail shelf space in Alberta is controlled by private companies and not government as in other provinces.

In those provinces there are government imposed structural impediments and additional economic costs levied against Alberta brewers. We do not support the concept of government imposed structural impediments as we do not believe that it is right for Alberta.

We do however believe that Alberta should only apply the graduated mark-up program to beer that is physically brewed in Alberta and that producers from outside the Province should pay the maximum rate. This will not restrict out-of-province brewers from selling their product in the Alberta market. Applying the graduated mark-up program only to brewers physically brewing their beer in Alberta will increase the viability of the local brewing industry, allowing for increased production, employment and local raw material sourcing. This in turn will generate higher associated tax revenue due to higher local economic activity.

Based on the historical beer sales volume data we have received, we estimate that the value of potential additional mark-up revenue that could accrue to the Province under a made-in-Alberta requirement would total approximately \$12.4 million per year.

- 2) Alberta's homegrown, small brewers generate substantial economic benefits to Alberta.

The signatories to this letter directly employ 1,185 full and part time people in brewing, sales, marketing, administration, retail and supply chain, with an estimated 100 spin-off jobs in other sectors we rely on for support and raw material inputs. The direct economic benefits to the province are almost \$36 million annually, with additional indirect spending to support Alberta's small brewers estimated to be another \$9 million, for a total economic benefit of \$45 million per year.

And this is in addition to the AGLC mark-ups paid by Alberta's small brewers. That's over 1,200 well-paying direct and indirect jobs and \$45 million of economic benefits. We believe that this represents an excellent return on investment with respect to the current graduated mark-up program and suggest that any changes made should be to encourage more growth in local brewing. Our review of small batch, handcrafted brewing producers in other provinces, such as Ontario and various states in the U.S., corroborates the notion that small brewers have a big impact in terms of job creation and economic activity as compared to the big beer industry.

We would be happy to share the results of these studies with you, as we also believe that Alberta's small brewers create more direct and indirect employment in this province than Molson and Labatt combined, due to our local activities and sourcing and our handcrafted, batch beers which are far more labour intensive to produce. One recent U.S. study ⁽¹⁾ found that small batch brewers in that country brewed 112 barrels per employee, while the giant beer factories run by one of the multinationals, AB InBev, brew 2,888 barrels per employee.

- 3) Alberta's local beer industry needs your support to thrive.

Of the almost 2.7 million Hectolitres sold in the province last year, only 7% was produced by Alberta's small brewers. The reason for this, we believe, is quite obvious. It is more advantageous to set up a brewery in BC or Saskatchewan, where one can receive 'favoured son' status on the government controlled retail shelves. British Columbia and Saskatchewan brewers enjoy the same mark-up system in Alberta as local producers do. Should the Alberta government be considering the potential application of the New West Partnership Trade Agreement in these circumstances, we assert that it will not enable Alberta's brewers the same access to retail shelf space in British Columbia and Saskatchewan that breweries based in those provinces enjoy in Alberta's free and open market. Honorable Minister Lukaszuk, the best way to get more small brewery start-ups and grow our local production is to put an end to this imbalance. We estimate that Alberta's trade deficit in beer is in the neighbourhood of \$500 million per year.

- 4) 'Tax cliffs' are an unjust and punitive construct.

The notion of retroactive taxation once a small brewer exceeds certain thresholds (currently 20,000 Hl and then 200,000 Hl in Alberta) ignores the job creation and economic benefits that far exceed the value of any foregone mark-ups and presumes erroneously that the breweries which exceed those thresholds actually have the ability to pay the retroactivity.

⁽¹⁾ *The Macroeconomics of Microbreweries - Scott Metzger, 01/2013*

We simply do not have that ability and would therefore not grow, but stagnate at those thresholds.

We reiterate the point, which was brought up in our previous letter, that retroactivity discourages the growth of, and investment in, small local breweries.

Honourable Deputy Premier Lukaszuk, we would like to finish by being as clear as possible as to our specific requests:

- 1) End the imbalance between Alberta and other provincial jurisdictions and put in place a made-in-Alberta requirement to qualify for the graduated mark-up policy. This will generate more revenue for the Province while still allowing completely unfettered access to retail shelves in Alberta - something Alberta producers do not enjoy in either province.
- 2) End the flawed and punitive notion of retroactive taxation. It inhibits job growth and investment and presumes that we could pay these taxes, which we cannot. We strongly suggest prospective application of any tax increases in Alberta so that we can have a growing job creating small beer industry.
- 3) Reduce mark-up rates at production levels below 50,000 hl to encourage investment in, and growth of, small breweries in Alberta, which will in turn contribute jobs and economic activity beyond the mere differential in mark-up taxation. The rate structure we proposed in our August 27, 2012 letter was:

	< 20,000 HI	20,000 HI to 50,000 HI	50,000 HI to 200,000 HI	200,000 to 400,000 HI	> 400,000HL
Alberta Producer	\$10.00/HI	\$20.00/HI	\$40.00/HI	\$98.00/HI	\$98.00/HI
Non-Alberta Producer	\$98.00 / HI	\$98.00 / HI	\$98.00 / HI	\$98.00 / HI	\$98.00 / HI

Alberta can have a growing, job-creating small beer industry if these changes are made. And we would again request a meeting at your earliest convenience to discuss our letter and any other issues that you may wish to explore.

We would be pleased to discuss the contents of this and our previous letter at your earliest convenience. Any of the following are available to respond on behalf of the group:

Alley Kat Brewing Company	Neil Herbst	(780) 436-8922
Big Rock Brewery	Bob Sartor	(403) 720-4457
Drummond Brewing	Kevin Wood	(403) 803-9543
The Grizzly Paw Brewing Co.	Robert Flatt	(403) 678-9983
Village Brewery	Stefan Horsky	(403) 651-9856

Respectfully,



Neil Herbst
ALLEY KAT BREWING COMPANY



Brett Ireland
(and on behalf of Alex Derksen/Socrates Korogonas)
BANFF AVENUE BREWING/
JASPER BREWING COMPANY



Bob Sartor
BIG ROCK BREWERY



Matt Lanigan
BREWSTERS BREWING COMPANY



Kevin Wood/Cody Geddes-Backman
DRUMMOND BREWING



Michele Lowney/Robert Flatt
(and on behalf of Niall Fraser)
THE GRIZZLY PAW BREWING COMPANY



Brian Molloy
HOG'S HEAD BREWING COMPANY



Al Gordon
RIBSTONE CREEK BREWERY



Stefan Horsky
VILLAGE BREWERY



Bill McKenzie/Jerry Chilibecki/Jim Brent
WILD ROSE BREWERY



WOOD BUFFALO BREWING CO.
Brett Ireland



YELLOWHEAD BREWING COMPANY
Bryce Parsons/Travis Boa

cc: The Honourable Alison Redford, M.L.A., Premier of Alberta
Encl.

August 27, 2012

Government of Alberta
408 Legislature Building
Edmonton, Alberta, T5K 2B6

Attn: Hon. Thomas Lukaszuk, Deputy Premier

Dear Mr. Lukaszuk:

RE: The Province's Graduated Mark-Up System

Meetings were held amongst senior representatives from 11 Alberta small brewers on August 15 & 20, 2012 at which recommended changes to the graduated mark-up system were discussed. Every brewer at that meeting brews their beer in Alberta, sources raw materials in Alberta and employs Albertans.

The graduated mark-up system was initially established to encourage the start-up and growth of a sustainable Alberta-based brewing industry. The current Alberta system is somewhat similar to programs in other parts of Canada and the United States, and was established in consultation with Alberta breweries. It was intended to place Alberta's small brewers on an even footing with brewers in other jurisdictions. At the time the current system was established, small Alberta brewers were struggling to stay in business, and indeed, by the time changes were made to the then existing flat tax system, six of the eleven existing small brewers had closed their doors, unable to compete. Since the current system was put in place, nine new breweries have either opened or are in advanced planning stages. Properly administered programs of this nature have a demonstrated ability to significantly grow the local brewing industry. The State of Oregon in the United States has a population of 3.8 million people and 121 craft breweries producing approximately 1.2 million hectolitres. The signatories to this letter number 11, producing just over 200,000 Hl for 3.6 million Albertans. With the right graduated mark-up system there is lots of room to grow.

- 1) Should the graduated mark-up program apply to beer that is not actually brewed in the Province of Alberta?

In an ideal world, where every Province provided brewers with a graduated mark-up program and had free, open and fair access to retail shelves, we would support applying the graduated mark-up program to all. But that is not the case as the market in Alberta is structurally unique on the Canadian landscape. Retail shelf space in Alberta is controlled by private companies and not Government as in other Provinces.

In those Provinces there are Government imposed structural impediments and additional economic costs levied against Alberta brewers. We do not support the concept of Government imposed structural impediments as we do not believe that it is right for Alberta.

.../Cont. 2

We do however believe that Alberta should only apply the graduated mark-up program to beer that is physically brewed in Alberta⁽¹⁾ and that producers from outside the Province should pay the maximum rate. This will not restrict out-of-Province brewers from selling their product in the Alberta market. Applying the graduated mark-up program only to brewers physically brewing their beer in Alberta will increase the viability of the local brewing industry, allowing for increased production, employment and local raw material sourcing. This in turn will generate higher associated tax revenue due to higher local economic activity.

- 2) Is the first tier (20,000 Hl) sufficient to encourage growth and start-ups in Alberta beer brewing or should there be additional tiers?

We urge the Government to establish a lower tier at 20,000 Hl or less at \$10.00 per Hl and a secondary tier from 20,000 Hl to 50,000 Hl at \$20.00 per Hl. We believe that this will spur investment in small craft breweries.

- 3) Once any tier is surpassed is it fair and reasonable to retroactively apply the higher mark-up to all production? Does this not have the effect of limiting growth in Alberta production to the benefit of the big multi-national players?

The retroactive application of the rates provides strong disincentive to exceed them. By way of example, an Alberta producer would, if the 200,000 Hl tier in Alberta were exceeded, have to produce over 300,000 Hl to just equal the 199,999 Hl level of profitability. At the Global 400,000 Hl level, the required volume bump to break even would be much higher. This punitive retroactive legislation directly benefits large multi-nationals who are already well above these levels and have a direct interest in limiting the growth of the local brewing industry.

On the Federal side, excise taxes are tiered with no retroactivity, precisely not to penalize growth. We believe the Provincial mark-ups should be handled in the same way.

- 4) Are other brewers using Alberta's fully open market and a graduated mark-up program to pump beer they produce that they cannot sell in their home markets in Alberta to keep their productivity levels high and costs per unit low?

The answer is yes. Some Canadian brewers, we believe, choose to sell excess production volume in the Alberta market because of the mark-up program incentives they receive. The incentives cover the extra costs of shipping and allow for a reduced price on their product in Alberta compared to their home markets, courtesy of the Alberta taxpayers. We strongly believe that beer brewed outside of the Province should be welcome in Alberta but should not be subsidized by the Alberta taxpayer. In Alberta, we currently have 46 other Canadian breweries that have listings in our Province and yet, we have only one local brewer that exports outside of the Province. Other Provinces' local breweries get automatic listings in their home markets in their provincially managed Government Liquor Stores.

⁽¹⁾ See Appendix 'A' for our definition of what constitutes an 'Alberta Brewery', 'Brewed in Alberta' and all of the graduated mark-up participants, and a suggested tier and mark-up table.

This gives these local breweries a great opportunity to gain market share and become established in their home markets. These non-Albertan breweries then take advantage of their home market stability, the mark-up incentive in Alberta, and the few barriers to entry into the Alberta market to compete with, and suppress Alberta producers here in Alberta.

We believe that some out of province breweries use the combination of the graduated mark-up system and low barriers to entry to sell their products more cheaply in Alberta than in their home markets. One example is from a Brewery based in British Columbia who is currently selling a 6-pack of beer in Alberta for \$5.99 including GST and deposit, whereas that same 6-pack in British Columbia is being sold at \$11.59 including taxes and deposit.

Today, Alberta breweries attempting to sell their products outside of Alberta do not receive the combination of a graduated mark-up system and low barriers to entry that non-Albertan breweries receive in the Alberta market.

Alberta craft brewers are overwhelmed with competition flocking into Alberta, encouraged by our free and open market and taxpayer-funded graduated mark-ups while our access to their markets are seriously curtailed by Provincial Government regulation in their home markets. We do not ask for Government intervention. We only ask that the Provincial Government does not encourage the flood of non-Albertan brewers' product coming into Alberta with reduced mark-ups and that this graduated mark-up review not result in changes that further debilitate an already stressed sector -- the small Alberta beer producers.

Honourable Deputy Premier Lukaszuk, we respectfully submit this letter on behalf of Alberta's Small Brewers and request an opportunity to meet with you and/or members of your staff to further discuss the matter.

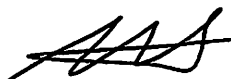
Respectfully,



Neil Herbst
ALLEY KAT BREWING COMPANY



Brett Ireland (and on behalf of Alex Derksen/Socrates Korogonas)
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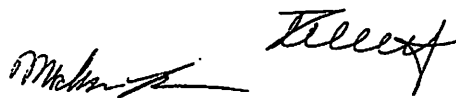
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BIG ROCK BREWERY



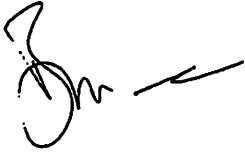
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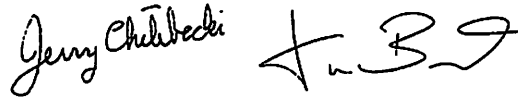
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WILD ROSE BREWERY



WOOD BUFFALO BREWING CO.
Brett Ireland

Attachment: APPENDIX 'A'

APPENDIX 'A'

ALBERTA BREWERY

A building or structure located within the boundaries of the Province of Alberta, facilitating the production of beer from malt, through wort production, fermentation and packaging.

BREWING IN ALBERTA

The production of beer from malt and hops by infusion resulting in a starch source that produces wort sugars which are then boiled, fermented and packaged in the Province of Alberta.

ALLOWABLE PARTICIPANTS

The graduated mark-up system should only apply to Alberta Breweries who brew in Alberta. If a brewery has both Alberta-based brewing and brewing in other non-Albertan locations, the graduated mark-up program on beer sold in Alberta should only apply to the volumes being brewed in Alberta.

SUGGESTED TIERS AND MARK-UP

	< 20,000 HI	20,000 HI to 50,000 HI	50,000 HI to 200,000 HI	200,000 to 400,000 HI	> 400,000HL
Alberta Producer	\$10.00/HI	\$20.00/HI	\$40.00/HI	\$98.00/HI	\$98.00/HI
Non-Alberta Producer	\$98.00 / HI	\$98.00 / HI	\$98.00 / HI	\$98.00 / HI	\$98.00 / HI