

BEER, LIQUOR, OR A LITTLE BIT OF BOTH? GETTING TO THE BOTTOM  
OF PROPERLY CLASSIFYING FLAVORED MALT BEVERAGES IN THE  
UNITED STATES AND AUSTRALIA

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## I. INTRODUCTION

Tax grab or genuine health policy? This is the question being asked of the movement towards taxing flavored malt beverages or “alcopops” at increasingly higher levels in Australia and the United States.<sup>1</sup> Alcopops are sweetened alcoholic beverages that are designed to mimic the flavor of lemonades, juices, and teas, and as such are more attractive to young persons.<sup>2</sup> Some popular examples include Mike’s Hard Lemonade, Barcardi Silver, Zima, and Smirnoff Ice.<sup>3</sup> These beverages typically contain the same amount of alcohol as beer (4% to 7%).<sup>4</sup> Moreover, the brewing process is initially the same for alcopops as it is for beer, but the end product typically contains an influx of distilled spirits or distilled spirit flavoring.<sup>5</sup> Since this is a hybrid beverage that is not easily labeled as “beer” or as a “distilled spirit,” taxation presents a complex issue.

This Note analyzes the progress of alcopop taxation in Australia and the United States. The objective of this Note is to answer several questions that arise when approaching the issue of alcopop taxation. First, should the process of beverage creation really determine its classification for tax purposes or should alcohol content be the determining factor? Second, is the concern of protecting some children from alcohol consumption an adequate reason to reclassify the tax status for alcopops? Third, is the taxation of alcopops a truly effective method for the prevention of underage drinking, or will teens simply turn to different alcoholic beverages?

To answer these questions, this Note takes an extensive look at the history of alcopops, evaluates the relevant arguments for and against taxation,

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<sup>1</sup> The term “alcopop” will be used to refer to “flavored malt beverages.” Definitions vary, but the California Board of Equalization provides a generalized summation:

The term Flavored Malt Beverage (FMB) is limited to an alcoholic beverage that is (1) produced from an initial fermented malt (or barley, hops, or other similar product) beverage base that is (2) treated to remove the basic malt beverage characteristics (e.g., color, bitterness, taste, etc.) and which (3) certain flavorings or other ingredients containing distilled alcohol are added . . . .

Memorandum from David J. Gau, Deputy Dir., Prop. & Special Taxes Dep’t, to Ramon J. Hirsig, Exec. Dir., Prop. & Special Taxes Dep’t (Feb. 26, 2009), *available at* [http://www.boe.ca.gov/meetings/pdf/ItemP3b1\\_\\_031709.pdf](http://www.boe.ca.gov/meetings/pdf/ItemP3b1__031709.pdf).

<sup>2</sup> VT. DEP’T OF LIQUOR CONTROL, STUDY TO IDENTIFY THE BEST PRACTICES FOR THE MARKETING, SALE, AND TAXATION OF MALT-BASED BEVERAGES CONTAINING OTHER INGREDIENTS SUCH AS FLAVORED DISTILLED SPIRITS, AND “ALCOHOL ENERGY DRINKS” 3 (2009), *available at* <http://www.leg.state.vt.us/reports/2009ExternalReports/240268.pdf>.

<sup>3</sup> *Id.* at 6.

<sup>4</sup> *Id.*

<sup>5</sup> *Alcopops Q & A*, CALIF. DEP’T OF ALCOHOL & DRUG PROGRAMS, <http://www.adp.ca.gov/youth/alcopops.shtml> (last visited Mar. 20, 2011).

examines the legislative histories of current alcopop taxation laws, and offers conjecture about what the best possible approach should entail.

Part II of this Note briefly discusses what an alcopop is and why their taxation is a significant issue for governments, for reasons of both public health and revenue. Part III evaluates the arguments for higher taxation of alcopops and, in doing so, explores how alcopops are created and marketed. Part IV addresses the relevant law in both Australia and the United States. This Note also examines the social, economic, and business aspects of the alcopop tax, as well as the differing strategies employed by alcoholic beverage companies to lobby against it. Finally, Part V attempts to answer the questions of what the appropriate classification is for alcopops, whether an increase in taxation is the best approach, and if there are any viable alternatives.

It is the position of this Note that the movement to classify alcopops in the same manner as distilled spirits, for tax purposes, will not be a complete success in the United States, as it has been in Australia. An initial hurdle in the United States is that the alcopop tax faces approval on a state-by-state basis, as opposed to Australia, where passage of the tax was done on a national level. While the number of states placing a higher tax on alcopops will likely increase, the legislation will serve more to increase state budgets than to combat the real issue of alcohol consumption by youths.

## II. ALCOPOPS AND THEIR IMPORTANCE

Introduced in the United States in the late 1980s, alcopops have been primarily lumped into the same category as beer for taxation purposes.<sup>6</sup> This was because they were typically made by beer breweries, packaged in the same sized bottles, and contained roughly the same amount of alcohol.<sup>7</sup> In addition to being taxed like beer, alcopops were also sold and advertised in the same manner.<sup>8</sup> The Vermont Department of Liquor succinctly concluded that alcopops “do not fit neatly into any existing alcohol categories and are currently classified improperly under Vermont law” and that “[a] separate definition for flavored malt beverages and alcohol energy drinks needs to be created . . . .”<sup>9</sup>

Both Australia and the United States continue to struggle with underage drinking.<sup>10</sup> The general idea behind a higher tax classification for alcopops

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<sup>6</sup> VT. DEP'T OF LIQUOR CONTROL, *supra* note 2, at 6.

<sup>7</sup> *Id.*

<sup>8</sup> *Id.*

<sup>9</sup> *Id.* at 4–5.

<sup>10</sup> See Ted R. Miller et al., *Societal Costs of Underage Drinking*, 67 J. STUD. ON ALCOHOL 519, 519 (2006) (“Underage drinking accounted for at least 16% of alcohol sales in 2001. It

is that it will discourage underage consumption and produce greater tax revenue on a product that purportedly imposes great societal costs.<sup>11</sup> With the recent downturn in the economy and the weak state of governmental budgets,<sup>12</sup> one would assume that this tax is attractive to legislators in an effort to protect youth and fill the proverbial coffers. However, not all of the legislators have been as enthusiastic about these possibilities, as some have called it a “blatant tax grab.”<sup>13</sup> Some studies in the United States suggest that U.S. taxes on alcohol generally have lagged greatly behind inflation.<sup>14</sup> One such study states that on a federal level, “in order to offset inflation just since 1991, the tax on distilled spirits would have to increase approximately \$20 per proof-gallon today and the tax on beer would have to increase to more than \$26.50 per barrel.”<sup>15</sup> Furthermore, the Center for Science in the Public Interest notes that the federal alcohol excise tax has only been raised once in fifty-five years.<sup>16</sup> In the twenty years leading up to 2004, only twenty-eight states have raised beer taxes, the same category under which alcopops are classified.<sup>17</sup> In its National Drug Strategy, the Australian government notes that although it has not recently studied its country’s responsiveness to price controls on alcohol, reliable international research supports this elastic approach.<sup>18</sup> “[T]here is strong research evidence that the Australian Government has, in its tax instruments, a very potent tool to

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led to 3,170 deaths and 2.6 million other harmful events. The estimated \$61.9 billion bill . . . included \$5.4 billion in medical costs, \$14.9 billion in work loss and other resource costs, and \$41.6 billion in lost quality of life.”); *see also Alcohol Pressuring Hospitals: Study*, CHRON. (Sept. 23, 2009), <http://www.thechronicle.com.au/story/2009/09/23/alcohol-pressuring-hospitals-research/> (asserting that “social dysfunction resulting from alcohol abuse is costing the economy at least \$15 billion a year”).

<sup>11</sup> DRUG-FREE ACTION ALLIANCE, *PROPERLY CLASSIFYING AND TAXING ALCOPOPS 3* (2007), available at <http://www.drugfreeactionalliance.org/files/alcopopsfinal.pdf>.

<sup>12</sup> *See* ELIZABETH McNICHOL ET AL., *STATES CONTINUE TO FEEL RECESSION’S IMPACT* (2011), available at <http://www.cbpp.org/files/9-8-08sfp.pdf> (noting that at the end of the first quarter of 2011, state tax revenues were down 9% due to the recession); *see also* Judy Lin, *10 States Face Looming Budget Disasters: Pew Report*, HUFFINGTON POST (Nov. 11, 2009), <http://www.huffingtonpost.com/2009/11/11/10-states-face-looming-budget-disasters-pew-report/> (citing a report that found ten states were “barreling toward economic disaster”).

<sup>13</sup> Matthew Franklin, *Senate Threat to Alcopop ‘Tax Grab,’* AUSTRALIAN (May 15, 2008), <http://www.theaustralian.com.au/senate-threat-to-alcopop-tax-grab/story-e6frgczf-111116343203>.

<sup>14</sup> CTR. FOR SCI. IN THE PUB. INTEREST, *THE CASE FOR ALCOHOL EXCISE TAX INCREASES 1* (2007), available at <http://www.cspinet.org/booze/taxguide/AlcoholTaxIncreases.pdf>.

<sup>15</sup> *Id.* at 2.

<sup>16</sup> *Id.*

<sup>17</sup> CENTER FOR SCI. IN THE PUB. INT., *FACTBOOK ON STATE BEER TAXES 8* (2004), available at <http://www.cspinet.org/booze/taxguide/040802BeerReport.pdf>.

<sup>18</sup> DEP’T OF HEALTH & AGING, *THE AVOIDABLE COSTS OF ALCOHOL ABUSE IN AUSTRALIA AND THE POTENTIAL BENEFITS OF EFFECTIVE POLICIES TO REDUCE THE SOCIAL COSTS OF ALCOHOL 14* (2008), available at [http://www.health.gov.au/internet/drugstrategy/publishing.nsf/Content/0A14D387E42AA201CA2574B3000028A8/\\$File/mono70.pdf](http://www.health.gov.au/internet/drugstrategy/publishing.nsf/Content/0A14D387E42AA201CA2574B3000028A8/$File/mono70.pdf).

influence alcohol prices, and therefore alcohol demand.”<sup>19</sup> Doctor Steven Skov of the Royal Australasian College of Physicians Alcohol Advisory Group argued in an editorial to the *Medical Journal of Australia* that a tax on alcopops is important but only a first step in expanding comprehensive tax reform on alcohol.<sup>20</sup> Further, Dr. Skov asserts that “[u]sing the tax system to influence pricing is by far the most effective and cost-effective single intervention to reduce the amount of alcohol that is drunk and the harm it causes.”<sup>21</sup>

Australia and the United States are not the first two countries to consider the taxation of alcopops as a possible solution to the perceived negative effects of alcopops. During the late 1990s, alcopops rapidly gained popularity in England, Scotland, Wales, and later Scandinavia, continental Europe, and Mediterranean countries.<sup>22</sup> Evidence exists that “the arrival of alcopops on to the market [in Wales] has been a factor in encouraging a new group of young drinkers to develop a regular drinking habit at an age earlier than might otherwise have been the case.”<sup>23</sup> The review by Metzner and Kraus<sup>24</sup> cites other work that suggests the introduction of alcopops is responsible for the overall increase in alcohol consumption by adolescents.<sup>25</sup> Additionally, studies indicate girls prefer alcopops more often than boys and specifically young girls choose alcopops over other alcoholic beverages.<sup>26</sup> Regarding taxation, the review notes that alcopop taxation in Germany and Switzerland resulted in a moderate decline in consumption, although Austria showed a similar decline without imposing a tax.<sup>27</sup>

Gabriel Romanus takes an in-depth look at another European country, Sweden, and the effects of alcopop introduction in 1996.<sup>28</sup> Romanus cites data that clearly suggests, “the introduction of alcopops [and] sweet ciders have contributed substantially to [increasing alcohol consumption by youth

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<sup>19</sup> *Id.*

<sup>20</sup> Steven J. Skov, *Alcohol Taxation Policy in Australia: Public Health Imperatives for Action*, ELEC. MED. J. AUSTL. (Mar. 16, 2009), [http://www.mja.com.au/public/issues/190\\_08\\_200409/sko10279\\_fm.pdf](http://www.mja.com.au/public/issues/190_08_200409/sko10279_fm.pdf).

<sup>21</sup> *Set Minimum Price for Alcohol, Reintroduce Alcopops Tax*, AUSTRALIAN MED. ASS'N (June 14, 2009), <http://ama.com.au/node/4746>.

<sup>22</sup> Cornelia Metzner & Ludwig Kraus, *The Impact of Alcopops on Adolescent Drinking: A Literature Review*, 43 ALCOHOL & ALCOHOLISM 230, 230 (2008).

<sup>23</sup> Chris Roberts et al., *The Impact of 'Alcopops' on Regular Drinking by Young People in Wales*, 6 DRUGS: EDUC., PREVENTION & POL'Y 7, 13 (1999).

<sup>24</sup> Metzner & Kraus, *supra* note 22, at 231–34.

<sup>25</sup> See, e.g., Gabriel Romanus, *Alcopops in Sweden—A Supply Side Initiative*, 95 ADDICTION S609, S618 (2000) (noting both substitution for other alcoholic beverages as well as increased consumption generally).

<sup>26</sup> Roberts et al., *supra* note 23, at 13.

<sup>27</sup> Romanus, *supra* note 25.

<sup>28</sup> *Id.* at 609.

groups and with greater consumption than the general public], and to an earlier drinking debut in the youngest age groups.”<sup>29</sup> However, he goes on to note, that a reduction in retail sales occurring later could be due to public debate and criticism of the product.<sup>30</sup> The Marin Institute, an alcohol industry watchdog, strongly supports such taxes and points to the purported success of the European model as a path for the United States and other countries to take.<sup>31</sup> The Institute specifically cites tax data from the United Kingdom, Germany, and Switzerland to argue that increased taxes have decreased alcopop consumption and underage drinking in general.<sup>32</sup>

It is important to note that public health groups drive much of the available research in this field. As a result, there is limited research concluding that alcohol taxes should remain static or be reduced. One such report was published in 2008 by the Distilled Spirits Industry Council of Australia.<sup>33</sup> The report takes a data driven approach in order to clarify many perceived myths about the alcopop industry in Australia.<sup>34</sup> Similar arguments against increased alcohol taxes can be found in the United States from the Distilled Spirits Council of the United States.<sup>35</sup> The Council’s website, which is aimed at stopping hospitality taxes, explores the negative effects on the industry and alcohol drinking populace.<sup>36</sup> The alcohol lobby in

<sup>29</sup> *Id.*

<sup>30</sup> *Id.* at 609, 618.

<sup>31</sup> *Taxing Alcopops as Distilled Spirits = Less Underage Drinking – European Data Makes Strong Connection*, ALCOHOL JUSTICE, <http://www.marininstitute.org/campaigns/stop-alcopop/10-alcopop-taxes-work-the-european-model.html> (last updated Jan. 22, 2009).

<sup>32</sup> *Id.*

<sup>33</sup> DISTILLED SPIRITS INDUS. COUNCIL OF AUSTL., SUBMISSION TO THE STANDING COMMITTEE ON COMMUNITY AFFAIRS: INQUIRY INTO READY TO DRINK ALCOHOL BEVERAGES (RTDs) 65 (2008), available at [http://www.aph.gov.au/senate/committee/clac\\_ctte/alcohol\\_beverages/submissions/sub27.PDF](http://www.aph.gov.au/senate/committee/clac_ctte/alcohol_beverages/submissions/sub27.PDF).

<sup>34</sup> *Id.* This report addressed seven facts aimed at resolving perceived industry myths:

Fact 1: Adult per capita alcohol consumption in Australia has fallen below 1970’s and 1980’s levels. Fact 2: There has been no significant increase in adult per capita alcohol consumption after tax reform (1 July 2000). Fact 3: Total alcohol consumption has been increasing at a lower rate than the 15 years and over population. Fact 4: Adult per capita consumption of RTDs has been growing as adult per capita consumption of beer and spirits has been falling. Fact 5: RTDs have similar alcohol content as beer but pay higher tax per volume of alcohol. Fact 6: RTDs comprise only 11% of the Australian alcohol market. Fact 7: 75% of RTDs are dark spirit-based, and are preferred by males 24 years and older.

*Id.*

<sup>35</sup> *The Federal Excise Tax on Beverage Alcohol*, DISTILLED SPIRITS COUNCIL OF THE U.S., <http://www.stophospitalitytaxes.com/join-the-fight/> (last visited Mar. 20, 2011).

<sup>36</sup> *Id.*

both the United States and Australia will likely fight any proposed increase in taxation, including the reclassification of alcopops as distilled spirits.<sup>37</sup>

There appears to be a consensus among studies that alcohol taxation has long remained too low given the societal costs that alcohol consumption may have inflicted.<sup>38</sup> The societal costs are not easily overlooked as the numbers can be staggering.<sup>39</sup> It is an issue that countries around the world have dealt with and one that has been brought to the forefront with recent legislative action in the United States and Australia.<sup>40</sup> The policy discussion regarding the proper method of taxation is one that will likely continue and will leave billions of dollars hanging in the balance.<sup>41</sup> Now that the significance of this issue has been demonstrated, this Note introduces the specific arguments addressing why alcopops should be placed within a higher tax classification.

### III. THE ARGUMENT FOR HIGHER TAXATION

The movement for placing alcopops into a higher taxation category is premised on two central arguments. First, alcopops are not actually beer and they are avoiding appropriate tax liability because of this improper classification.<sup>42</sup> Second, alcopops intentionally target underage consumers, and thus, higher taxes would discourage consumption.<sup>43</sup> The reclassification

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<sup>37</sup> See *California Product Testing for Alcopops Advances*, ALCOHOL JUSTICE, <http://www.marininstitute.org/campaigns/stop-alcopops/214-product-testing-implementation-plan-for-flavored-malt-beverages.html> (last updated Mar. 20, 2011) (reporting on the alcohol industry's fight for favorable tax classification in California); see also Mark Metherell, *Tax on Alcopops Sets Off Alcohol Lobby War*, SYDNEY MORNING HERALD (June 12, 2008), <http://www.smh.com.au/news/national/tax-on-alcopops-sets-off-alcohol-lobby-war/2008/06/11/1212863740798.html> (discussing the fresh lobbying war created by the proposition of further tax changes for alcohol).

<sup>38</sup> See, e.g., Philip J. Cook & Michael J. Moore, *The Economics of Alcohol Abuse and Alcohol-Control Policies*, 21 HEALTH AFF. 120, 130 (2002), available at <http://content.healthaffairs.org/content/21/2/120.full.pdf> ("Current excise-tax rates are too low, both nationally and in every state. The rates are far less than the average social cost of each drink consumed.").

<sup>39</sup> See generally *id.* at 126 (citing the Centers for Disease Control and Prevention which "estimated 'alcohol-related mortality' as 105,000 in 1987, 4.9 percent of all deaths in that year").

<sup>40</sup> See James F. Mosher & Dianne Johnsson, *Flavored Alcoholic Beverages: An International Marketing Campaign That Targets Youth*, 26 J. PUB. HEALTH POL'Y 326, 328–29 (2005) (noting the overall increase in global alcopop sales).

<sup>41</sup> See *The Federal Excise Tax on Beverage Alcohol*, *supra* note 35 (noting that the U.S. alcohol industry generates over \$350 billion of economic activity); see also Siobhain Ryan, *Middle-aged Men Outdrinking Teen Tipplers*, AUSTRALIAN (June 2, 2008), <http://www.theaustralian.com.au/news/nation/middle-aged-men-outdrinking-teen-tipplers/story-e6frg6nf-111116509336> (reporting that the alcopop tax hike will yield \$3.1 billion in tax revenue over five years).

<sup>42</sup> DRUG-FREE ACTION ALLIANCE, *supra* note 11.

<sup>43</sup> *Id.*; see also Mosher & Johnsson, *supra* note 40, at 326, 338 (citing the success of other countries in reducing underage consumption of alcopops upon increasing taxes).

of alcopops would also increase tax revenue, thereby beginning to cover the ostensible societal costs of alcopops.<sup>44</sup>

Opponents argue that alcopops are not similar to beer and should not be taxed as such.<sup>45</sup> This is an intricate argument based upon the complexity of the alcopop brewing process. According to the Internal Revenue Code, fermentation is the central criteria for determining what is and is not beer and alcopops blur this line.<sup>46</sup> The debate centers on whether alcopops should be taxed according to the percentage of alcohol or by the type of alcohol they contain.<sup>47</sup> The solution depends on what percentage of alcohol in alcopops is derived from fermentation in the brewing process and what percentage comes from added distilled spirits.<sup>48</sup> The alcohol industry has undoubtedly taken advantage of this blurred line in the United States by emphasizing the malt characteristics of alcopops and downplaying the addition of distilled spirits.<sup>49</sup> Smirnoff Ice, for instance, emphasizes its vodka content in the United Kingdom while it is touted as a malt beverage within the United States.<sup>50</sup>

In 2003, the United States Alcohol and Tobacco Trade and Tax Bureau (TTB) released a study about the production and makeup of alcopops.<sup>51</sup> It determined that alcopops do not resemble beer or malt beverages in the traditional sense.<sup>52</sup> Although alcopops are brewed from the same base as typical beers, those brewers remove all the characteristics generally associated with beer and then add flavoring.<sup>53</sup> Sometimes up to 99% of the alcohol within an alcopop is derived from added distilled spirits.<sup>54</sup> Since it is

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<sup>44</sup> Skov, *supra* note 20, at 2.

<sup>45</sup> See VT. DEP'T OF LIQUOR CONTROL, *supra* note 2 (stating that alcopops "do not fit into the traditional alcoholic beverage categories"); see also Flavored Malt Beverages and Related Proposals, 68 Fed. Reg. 14,292, 14,294 (proposed Mar. 24, 2003) (to be codified at 27 C.F.R. pts. 7, 25) [hereinafter Flavored Malt Beverages Proposal] (noting that the brewing process "not only sets flavored malt beverages apart from other malt beverages, but also raises the question of whether they should be classified as beer or as distilled spirits").

<sup>46</sup> Flavored Malt Beverages Proposal, *supra* note 45, at 14,294; Daniel Barlow, *Line Between Alcoholic, Non-alcoholic Drinks Blurred, Lawmakers Told*, TIMES ARGUS (Feb. 5, 2009), <http://www.timesargus.com/article/20090205/NEWS01/902050354>.

<sup>47</sup> See Flavored Malt Beverages Proposal, *supra* note 45 (discussing the proposed method of taxing alcopops).

<sup>48</sup> *Id.* (discussing the proper method of taxing alcopops).

<sup>49</sup> See Simon Rosen & Michele Simon, *Alcopops in the United States: State by State Battle to End Corporate Tax Fraud*, 2 GLOBE 25, 25 (2008), available at <http://www.ias.org.uk/resources/publications/theglobe/globe200802/gl200802.pdf> (arguing that the alcopop industry is committing "corporate tax fraud").

<sup>50</sup> *Id.*

<sup>51</sup> Flavored Malt Beverages Proposal, *supra* note 45.

<sup>52</sup> *Id.*

<sup>53</sup> *Id.*

<sup>54</sup> *Id.*



initially brewed from malt, the product technically fits within the definition of “beer.”<sup>55</sup> The TTB determined though, that the majority of alcopops derive their alcohol content from added distilled spirits.<sup>56</sup> The TTB’s opinion is that since the alcohol content of alcopops comes largely from distilled spirits, it was not properly classified in the malt beverage category.<sup>57</sup> The TTB specifically found that “to label a beverage that derives most of its alcohol content from added alcohol flavors as a malt beverage is inherently misleading since consumers would expect that malt beverages derive a significant portion of their alcohol content from fermentation of barley malt and other ingredients at the brewery.”<sup>58</sup> The TTB proposal and eventual regulation that became effective in January 2006 allows the taxation of alcopops like beer as long as they contain less than 6% alcohol and derive no more than 49% of their alcohol from added distilled spirits.<sup>59</sup> While most alcopops contain around 6% alcohol content, only four of the 114 alcopops tested by the TTB would pass this new regulation.<sup>60</sup>

The TTB selected 49% due to its use as the historical dividing line for alcohol taxation purposes.<sup>61</sup> In the period after the TTB’s initial proposal, the TTB solicited comments and some organizations, such as the National Consumer League (the League), attacked the arbitrariness of the 49% standard.<sup>62</sup> In its letter, “the League” argued that distinguishing between alcohol based on fermentation or distillation misleads the consumer.<sup>63</sup> The

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<sup>55</sup> *Id.*

<sup>56</sup> *Id.*

<sup>57</sup> *Id.*

<sup>58</sup> *See id.* at 14,296 (finding that out of 114 malt beverages sampled, 105 derived between 76% and 99.98% of their alcohol content from distilled spirits, five derived between 51% and 75% of alcohol content from distilled spirits, four were between 0% and 25%, and only fifteen of the 114 beverages tested derived even half of their alcohol content from fermentation).

<sup>59</sup> Labeling and Advertising of Malt Beverages, 27 C.F.R. § 7.11 (2005). The amended regulation provides the following:

Flavors and other nonbeverage ingredients containing alcohol may be used in producing a malt beverage. Except as provided in paragraph (a)(2) of this section, no more than 49% of the overall alcohol content of the finished product may be derived from the addition of flavors and other nonbeverage ingredients containing alcohol. For example, a finished malt beverage that contains 5.0% alcohol by volume must derive a minimum of 2.55% alcohol by volume from the fermentation of barley malt and other materials and may derive not more than 2.45% alcohol by volume from the addition of flavors and other nonbeverage ingredients containing alcohol.

*Id.*

<sup>60</sup> Flavored Malt Beverages Proposal, *supra* note 45, at 14,294.

<sup>61</sup> *Id.*

<sup>62</sup> Letter from Linda F. Golodner, President, Nat’l Consumers League to Chief of Regulations & Procedures Div., Alcohol & Tobacco Tax & Trade Bureau (Aug. 15, 2003), *available at* [http://www.ttb.gov/nprm\\_comments/ttb\\_comments\\_4/comments/pdf/0040779.pdf](http://www.ttb.gov/nprm_comments/ttb_comments_4/comments/pdf/0040779.pdf).

<sup>63</sup> *Id.*

League argues that “TTB seems to be encouraging product reformulation of [alcopops] on the assumption that products with distilled spirit content are less preferable than those with malt beverage content . . . . The source of that alcohol is simply not material, and TTB should cease attempting to formulate public policy on this basis.”<sup>64</sup>

The Food Marketing Institute (the Institute) points out that alcopops contain roughly the same alcohol content as beer, and brewers of alcopops have been unrestrained in adding alcohol flavoring for more than two decades.<sup>65</sup> The Institute disagrees with the TTB’s contention of consumer deception as it claims that “the supermarket industry believes adult consumers are both knowledgeable about flavored malt beverages and fully understand that they have much lower alcohol content than distilled spirits.”<sup>66</sup>

More important to producers of alcopops is that classification as a distilled spirit would prevent the sale of alcopops sold in many grocery stores across the country, severely impacting the beverage’s profitability.<sup>67</sup> Despite arguments against their positions, the TTB maintains that the dividing line between beer and distilled spirits should not be premised on the overall alcohol percentage of the beverages, but rather by the percentage of alcohol in the beverage derived through fermentation versus from distilled spirits.<sup>68</sup>

Many Australians have voiced similar concerns.<sup>69</sup> For example, writing for TaxWatch.org in Australia, University of Melbourne Professor John Freebairn argues that the only reasonable approach to an alcohol excise tax is to apply a standard rate based upon the volume of the alcohol, independent of the beverage type.<sup>70</sup> Mr. Freebairn states, “[i]deally, a common rate of tax per litre of alcohol would be levied on all forms of alcohol and be set at the level necessary to reduce and then meet the external costs.”<sup>71</sup>

The second impetus for a tax on alcopops is that the beverages specifically target youth consumers.<sup>72</sup> Studies have repeatedly demonstrated that younger drinkers prefer alcopops to other alcoholic beverages.<sup>73</sup> The

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<sup>64</sup> *Id.*

<sup>65</sup> Letter from John J. Motley III, Senior Vice President, Food Marketing Inst., to Chief of Regulations & Procedures Div., Alcohol & Tobacco Tax & Trade Bureau (July 7, 2003), available at <http://www.fmi.org/newsletters/uploads/CommentsFiled/MaltbeverageComments7-03.pdf>.

<sup>66</sup> *Id.*

<sup>67</sup> Mosher & Johnsson, *supra* note 40, at 334.

<sup>68</sup> 27 C.F.R. §§ 7, 13–14, 25; Flavored Malt Beverages Proposal, *supra* note 45, at 14,295.

<sup>69</sup> John Freebairn, *Beyond Alcopops: The Case for Beverage Equity*, TAX WATCH (May 21, 2009), [http://www.taxwatch.org.au/talk.asp?id=3#Byeond\\_Alcopops](http://www.taxwatch.org.au/talk.asp?id=3#Byeond_Alcopops).

<sup>70</sup> *Id.*

<sup>71</sup> *Id.*

<sup>72</sup> Mosher & Johnsson, *supra* note 40.

<sup>73</sup> E.g., Jan Copeland et al., *Young Australians and Alcohol: The Acceptability of Ready-to-*

added flavoring of alcopops reduces the typically strong taste and odor of alcohol, making alcohol more palatable for younger drinkers.<sup>74</sup> Mosher and Johnsson describe alcopops as “relatively low alcohol content beverages that are designed for ‘entry level’ drinkers.”<sup>75</sup> In particular, teenaged girls are said to be the primary targets.<sup>76</sup> In a press release, DrugFreeAlliance.org confirmed this, citing an American Medical Association study released in 2004 that found 31% of teenaged girls had consumed alcopops within the past six months, compared to only 19% of teenage boys.<sup>77</sup> Additionally, the press release refers to a study by the Center for Alcohol Advertising and Youth that found that “girls ages 12–20 saw 95% more magazine ads for alcopops than women over 21. Women 21–34, the age group identified as the target audience for alcohol ads, were actually less exposed per capita to magazine advertising for alcopops and beer than girls aged 12–20.”<sup>78</sup>

The studies discussed above clearly indicate that alcopop advertising is reaching a wide audience, including teenagers, and the products themselves have acquired a foothold with a younger population.<sup>79</sup> It is important to note that the tax status of alcopops enables them to maintain this position in several ways.<sup>80</sup> Enjoying the same tax classification benefits as beer allows alcopops to be “(1) advertised on electronic media; (2) taxed at substantially lower tax rates; and (3) available in a greater number of retail locations, particularly those likely to be frequented by underage drinkers.”<sup>81</sup>

When seeking to answer the question of whether alcopops are specifically targeting minors through advertising, many take the approach of analyzing

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*Drink (RTD) Beverages Among 12-30-Year-Olds*, 102 ADDICTION 1740, 1745 (2007) (finding alcopops “to be more likeable than other types of alcohol among those aged under 18 years of age”).

<sup>74</sup> *Id.*

<sup>75</sup> Mosher & Johnsson, *supra* note 40.

<sup>76</sup> See *Teenage Girls Targeted for Sweet-Flavored Alcoholic Beverages*, ALCOHOLPOLICYMD.COM (Dec. 16, 2004) [hereinafter *Teenage Girls*], available at [http://www.alcoholpolicy.com/press\\_room/Press\\_releases/girlie\\_drinks\\_release.htm](http://www.alcoholpolicy.com/press_room/Press_releases/girlie_drinks_release.htm) (discussing the way marketers are targeting girls by developing sweet-flavored drinks).

<sup>77</sup> DRUG-FREE ACTION ALLIANCE, *supra* note 11.

<sup>78</sup> *Teenage Girls*, *supra* note 76; see also David H. Jernigan et al., *Alcohol Advertising and Youth: A Measured Approach*, 26 J. PUB. HEALTH POL’Y 312, 316 (2005) (stating “[g]irls who saw more alcopop and beer advertising per capita in magazines than women aged 21–34”).

<sup>79</sup> See, e.g., *Teenage Girls*, *supra* note 76; see also Jernigan et al., *supra* note 78 (addressing the ways in which alcohol companies can reduce “overall youth exposure to their advertising”).

<sup>80</sup> Mosher & Johnsson, *supra* note 40; see also JAMES F. MOSHER, *FLAVORED ALCOHOLIC BEVERAGES AND THE YOUTH MARKET* (2005), available at [http://www.alcoholpolicyconsultations.com/downloads/fab\\_briefing\\_paper-2-05.pdf](http://www.alcoholpolicyconsultations.com/downloads/fab_briefing_paper-2-05.pdf) (discussing the ways in which most alcopops are classified as “malt beverages” which allows them to be distributed and advertised on a larger scale than liquor and also allows them to be taxed at a lower rate).

<sup>81</sup> MOSHER, *supra* note 80; Mosher & Johnsson, *supra* note 40.

the “four P’s” of market strategy: product, promotion, placement, and price.<sup>82</sup> While the alcopop industry claims their products are aimed at new drinkers who are over the drinking age, the data suggests the average age of alcohol initiation is constantly dropping and was 15.9 years in 1999.<sup>83</sup> Exploring the increased advertising that has followed the rising sales of alcopops in the United States also indicates a “total marketing” scheme aimed at underage drinkers.<sup>84</sup> The industry has taken advantage of both traditional advertising, including television, radio, print, and outdoor advertising, as well as non-traditional, methods including internet advertisements, product placement, and event sponsorships.<sup>85</sup> Spending by alcopop companies on both traditional and non-traditional advertising was estimated at over \$600 million in 2002 alone and<sup>86</sup> younger consumers are inevitably exposed to this large amount of advertising.<sup>87</sup>

Placement concerns for the alcopop industry are enormous with tax classification in mind because most current classifications keep alcopops in beer retail outlets opposed to distilled spirits outlets.<sup>88</sup> In the United States there are three times as many beer outlets as distilled spirits outlets, so the importance becomes obvious.<sup>89</sup> Studies show that there is a similar ratio of beer and distilled spirit sellers throughout the world.<sup>90</sup>

Price is the final component of the purported total marketing scheme aimed at underage drinkers.<sup>91</sup> It is argued that youth are very price sensitive and this makes avoiding the higher tax rates of distilled spirits, sometimes up to five to ten times higher, very critical for the alcopop industry.<sup>92</sup> The importance in avoiding this higher tax rate proved critical for fringe beverages in the past such as wine coolers, which suffered a decline in sales after their applicable tax rate increased.<sup>93</sup> This beer or distilled spirits tax distinction exists throughout the world.<sup>94</sup>

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<sup>82</sup> Mosher & Johnsson, *supra* note 40, at 331. The product design that is particularly conducive to entry-level drinkers has been significantly discussed up to this point and thus will not be addressed in the four part analysis.

<sup>83</sup> *Id.* at 332.

<sup>84</sup> *Id.* at 331–33.

<sup>85</sup> *Id.* at 333.

<sup>86</sup> *Id.*

<sup>87</sup> *See id.* at 334 (citing a survey that found teenagers are more than three times as likely as adults to be exposed to alcopops through advertising).

<sup>88</sup> *Id.*

<sup>89</sup> *Id.*

<sup>90</sup> *Id.*

<sup>91</sup> *Id.* at 335.

<sup>92</sup> *Id.*

<sup>93</sup> *Id.*

<sup>94</sup> *Id.*

#### IV. THE LAW

An examination of the specific Australian alcopop legislation serves as a useful tool in analyzing the overall movement. The history of the proposed tax in Australia, from its inception to its ultimate death provides an insight into the social, economic, and political factors that will likely be important when American states consider this tax. While a direct comparison between the two countries for purposes of evaluating the tax's possible success or failure in the United States would be imprudent given the dichotomy of the relationship between federal and state governments within the United States, this Note argues that the tax faces too many challenges to truly succeed in its mission.

##### A. *The Law in Australia*

The relevant taxation power in Australia for purposes of this Note is the "excise tax." This excise power was transferred to the new Commonwealth Government upon Federation in 1901.<sup>95</sup> Parliament holds the exclusive power to levy an excise tax.<sup>96</sup> Excise taxes are duties levied on certain types of domestically produced goods such as alcohol, petroleum, and tobacco.<sup>97</sup> Manufacturers, not retailers, generally pay excise taxes.<sup>98</sup> Australian courts broadly define the term "excise" and even prevent states from imposing sales taxes.<sup>99</sup> Effecting change in excise taxes is a process in Australia unlike anything in the United States.<sup>100</sup> Collection typically occurs before the actual "implementing legislation" passes.<sup>101</sup> "Tariff proposals" allow the government to begin collecting taxes instantly while the legislation is

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<sup>95</sup> *Australian Tax History*, AUSTRALIAN TAXATION OFFICE (Apr. 7, 2003), [http://www.ato.gov.au/corporate/content.asp?doc=/content/tax\\_history.htm](http://www.ato.gov.au/corporate/content.asp?doc=/content/tax_history.htm).

<sup>96</sup> See AUSTRALIAN CONSTITUTION s 90 (giving Parliament the power to impose customs and duties and extinguishing existing customs or duties levied by states).

<sup>97</sup> *Australian Tax History*, *supra* note 95. The fact that these taxes are placed at the top of the chain rather than at the bottom with the retailers certainly contributes to the insistence of the industry lobby. *Id.*

<sup>98</sup> *Id.*

<sup>99</sup> See Neil Halliday, *Ha & Anor v State of New South Wales & Ors Walter Hammond & Associates v State of New South Wales & Ors: The Next Excise Tax Case Should Tell Whether Governments Can Look Forward to a Return to a Measure of Clarity and Unanimity on Section 90*, 20 SYDNEY L. REV. 158 (1998) (discussing the majority view in *Ha* that section 90 was intended to catch the entirety of state taxes because it was ultimately intended to give the Commonwealth complete control over fiscal policy), available at <http://www.austlii.edu.au/au/journals/SydLRev/1998/7.html>.

<sup>100</sup> See Andrew Hudson, *Australia: Alcopop Dispute Fizzes Out in the Federal Court*, HUNT & HUNT LAWYERS (Apr. 16, 2009), available at <http://www.mondaq.com/australia/article.asp?articleid=78110> (noting that while generally non-controversial, the process may not be legal).

<sup>101</sup> *Id.*

presented to Parliament.<sup>102</sup> This legal grey area becomes even murkier if the legislation being implemented is not passed within twelve months.<sup>103</sup> Those paying the tax cannot challenge the tariff proposal (if lacking implementing legislation) for twelve months, possibly resulting in “taxation without legislation,” where the government effectively collects a tax that does not legally exist.<sup>104</sup> If the twelve month deadline is reached without legislation, although rarely the case, the government would have to return the collected taxes.<sup>105</sup>

Australian Prime Minister Kevin Rudd’s move to nearly double the tax on alcopops in April 2008 was motivated by his plan to curb underage and youth binge drinking.<sup>106</sup> The resulting 70% excise tax increase resulted in alcopop prices rising between AU \$0.30 and AU \$1.30.<sup>107</sup> Expected revenues from the new taxes were AU \$3.1 billion.<sup>108</sup> The increase was part of the Prime Minister’s “National Binge Drinking Strategy” that specifically cites “[c]losing the dangerous tax break for alcopops, used to hook young girls on binge-drinking” as one of its goals.<sup>109</sup> The “tax break” that the plan refers to is the lower tax rate that was introduced in July of 2000.<sup>110</sup> This received an expected response; public health groups praised the increase and industry organizations questioned the effectiveness of the proposed tax increase.<sup>111</sup>

Specifically, the Excise Tariff Proposal (No. 1) 2008 and the Customs Tariff Proposal (No. 1) 2008 targeted “other excisable beverages not

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<sup>102</sup> *Id.*

<sup>103</sup> *See id.* (claiming that there would be several interesting legal questions if the twelve month deadline is reached before legislation is passed).

<sup>104</sup> *Id.*

<sup>105</sup> *Id.*

<sup>106</sup> Gisselle Gallego, *Doubling the Alcopop Tax*, HEALTH POL’Y MONITOR (2008), <http://www.hpm.org/survey/au/a12/4>.

<sup>107</sup> *Id.* In July of 2008, the AUD approached near parity with the USD with the equivalency of \$0.96 USD equaling \$1.00 AUD. By the end of the year in December, however, the ratio was down to \$0.67 USD equaling \$1.00 AUD. *Monthly Average Graph: American Dollars to 1 Australian Dollar 2008*, X-RATES.COM, <http://www.x-rates.com/d/USD/AUD/hist2008.html> (last visited Mar. 20, 2011).

<sup>108</sup> Gallego, *supra* note 106.

<sup>109</sup> Press Release, Honorable Nicola Roxon, Minister for Health and Ageing, National Binge Drinking Strategy (Nov. 17, 2008), *available at* <http://www.health.gov.au/internet/ministers/publishing.nsf/Content/mr-yr08-nr-nr156.htm>; *see also* Josh Gordon & Dan Harrison, *Booze Blitz: Alcopop Tax Lifted by 70%*, AGE (Apr. 27, 2008), <http://www.theage.com.au/articles/2008/04/27/1208743339515.html> (citing a 2007 survey compiled by the Australian Institute of Health and Welfare that found females, age twelve to fifteen years old, were three times more likely than males to consume alcohol one or more times per week).

<sup>110</sup> Gallego, *supra* note 106.

<sup>111</sup> *See id.* (citing the responses of organizations such as the Australian Drug Foundation, Public Health Association, and Diageo).

exceeding 10 per cent by volume of alcohol.”<sup>112</sup> The tariff proposals increase the tax “from [AU] \$39.36 to [AU] \$66.67 per litre of alcohol content,”<sup>113</sup> shifting alcopops into the same taxation category as distilled spirits.<sup>114</sup> The proposal claimed that the government planned to use part of the tax revenue to fund the country’s largest investment in preventative health, focusing on alcohol among other things.<sup>115</sup>

Beginning in April of 2008, the movement toward higher excise taxes continued to gain support for implementing legislation that was necessary for the tax increase to become permanent.<sup>116</sup> The Australian Drug Foundation and the Medical Journal of Australia both published studies citing the success of the tax.<sup>117</sup> Others, however, argued that the tax has simply pushed consumers away from alcopops and towards other types of alcohol.<sup>118</sup>

The study released by the Australian Drug Foundation, citing Neilson statistics, claimed that there was a 28% decrease in alcopops sales between May and January after the March implementation of the tax and seemed to prove the tax’s effectiveness.<sup>119</sup> This decrease followed seven years of growth in the alcopop category.<sup>120</sup> Another important finding of the study was the massive difference in alcopop consumption between the United States and Australia.<sup>121</sup> Australia tops all other countries in the world with

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<sup>112</sup> Summary of Alterations, Excise Tariff Proposal (No.1) 2008; Customs Tariff Proposal (No. 1) (2008) (Austl.), available at [http://www.aph.gov.au/library/pubs/explanmem/docs/2008ExciseTariffProposal\(no1\)alcopop.pdf](http://www.aph.gov.au/library/pubs/explanmem/docs/2008ExciseTariffProposal(no1)alcopop.pdf).

<sup>113</sup> *Id.*

<sup>114</sup> Josh Gordon & Dan Harrison, *Booze Blitz: Alcopop Tax Lifted by 70%*, AGE (Apr. 27, 2008), <http://www.theage.com.au/articles/2008/04/27/1208743339515.html>.

<sup>115</sup> *Id.*

<sup>116</sup> Hudson, *supra* note 100.

<sup>117</sup> See Tanya N. Chikritzhs et al., *The “Alcopops” Tax: Heading in the Right Direction*, 190 MED. J. AUSTL. 294 (2009), available at [http://www.mja.com.au/public/issues/190\\_06\\_160309/chil1362\\_fm.html](http://www.mja.com.au/public/issues/190_06_160309/chil1362_fm.html) (arguing that the tax is an effective and an important step in addressing the harm caused by alcohol); see also Press Release, Australian Drug Foundation, Price Matters: Alcopops Consumption Down (May 27, 2010) (on file with author) (citing a Neilson study that shows sales of alcopops have dropped by 310 million standard drinks).

<sup>118</sup> See Editorial, *Lies, Damned Lies, Statistics and Those Alcopops*, COURIER (July 29, 2008), <http://www.thecourier.com.au/news/opinion/editorial/general/lies-damned-lies-statistics-and-those-alcopops/1228813.aspx> (noting statistics from the Liquor Merchants Association of Australia that show while alcopop sales decreased by 30% since the tariff proposal, the sale of bottled spirits increased by 50%).

<sup>119</sup> Press Release, Australian Drug Foundation, Latest Figures Prove Alcopop Tax Is Hitting Home (Mar. 8, 2009) [hereinafter Australian Drug Foundation], available at <http://www.accessmylibrary.com/article-1G1-195110735/media-release-australian-drug.html>. The study shows an immediate decrease by percentage after the March tax of 18% in May. Through the Australian winter (June through August), alcopop sales hit their low, with as much as a 32% decrease. Even during the Australian summer, in December the figure still reached a 26% decrease in sales. *Id.*

<sup>120</sup> See *id.* (comparing RTD volumes in liters in 2000 and 2007, finding a compound annual growth of 10%).

<sup>121</sup> See *id.* (finding a twelve liter per person difference between Australians and Americans).

an average of fourteen liters of alcopops consumed per person, per year.<sup>122</sup> The United Kingdom consumes less with 6.7 liters per person and the United States has an even smaller consumption rate with only two liters per person.<sup>123</sup> Even going back to 1995, the Australian rate was still higher than that of the United States, hovering above 2.5 liters per person.<sup>124</sup> No other country studied saw growth in alcopop consumption comparable to that of Australia.<sup>125</sup> The study did concede a slight growth in spirit sales.<sup>126</sup>

In 2009, Parliament referred the alcopop tax to the Australian Senate Standing Committee on Community Affairs, which conducted an inquiry with a timeline of just over one month.<sup>127</sup> The committee accepted submissions, and two noteworthy submissions came from the National Drug Research Institute and Independent Distillers Australia.<sup>128</sup> In their submission, the National Drug Research Institute relied on the same Neilson studies as above, but noted that “[d]efinitive statements about the impact of the so-called ‘alcopops tax’ are premature in the absence of independent alcohol sales data.”<sup>129</sup> The report recognizes that its conclusion to support the legislation is based on only taxation data and the Neilson study.<sup>130</sup>

Conversely, the submission from Independent Distillers Australia presumes that the government’s proposed tax will fail to achieve its revenue and health policy objectives.<sup>131</sup> The report challenges the Treasury Department statistics that the National Drug Institute heavily relied on when formulating their submission.<sup>132</sup> Their attack is two-fold: First, Independent Distillers Australia presents evidence supporting the “substitution effect” and second, they attack the modeling underpinning the statistics.<sup>133</sup>

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<sup>122</sup> *Id.*

<sup>123</sup> *Id.*

<sup>124</sup> *Id.*

<sup>125</sup> *Id.* In fact, the United States maintained essentially static growth in alcopop consumption from 1995 to 2007.

<sup>126</sup> *Id.*

<sup>127</sup> DISTILLED SPIRITS INDUS. COUNCIL OF AUSTL., *supra* note 33.

<sup>128</sup> STEVE ALLSOP ET AL., NAT’L DRUG RESEARCH INST., THE IMPACT OF THE TAX ON READY-TO-DRINK ALCOHOLIC BEVERAGES (2008), [http://www.aph.gov.au/senate/committee/clac\\_ctte\\_excise\\_customs\\_tariff/submissions/sub05.pdf](http://www.aph.gov.au/senate/committee/clac_ctte_excise_customs_tariff/submissions/sub05.pdf); DISTILLED SPIRITS INDUS. COUNCIL OF AUSTL., *supra* note 33.

<sup>129</sup> ALLSOP ET AL., *supra* note 128.

<sup>130</sup> *Id.*

<sup>131</sup> INDEP. DISTILLERS AUSTL., SENATE INQUIRY INTO READY TO DRINK (RTD) ALCOHOLIC BEVERAGES 2 (2008).

<sup>132</sup> *Id.* The Neilson statistics supporting the success of the tax seem to be the primary study used by the tax advocates and shows up in many different sources. This study combined with Treasury projections make up the base of support for the tax. *Id.*

<sup>133</sup> DOUG MCKAY, SENATE INQUIRY INTO READY TO DRINK (RTD) ALCOHOLIC BEVERAGES: SUBMISSION FROM INDEPENDENT DISTILLERS IN AUSTRALIA 15, 20 (2008), *available at* [http://www.aph.gov.au/senate/Committee/clac\\_ctte/alcohol\\_beverages/submissions/sub22.pdf](http://www.aph.gov.au/senate/Committee/clac_ctte/alcohol_beverages/submissions/sub22.pdf).



The use of the substitution effect serving as an explanation for falling alcopop sales is a primary tool of attack for opponents of increasing the excise tax.<sup>134</sup> The submission claims that “there is clear evidence through retail sales data since the increase of the excise that there will be almost a direct substitution to beer, cider (same strength), wine (three times stronger) and spirits (seven to 10 times stronger).”<sup>135</sup> This statement is based upon data obtained from Chambers Cellars, a chain of independently owned retail liquor stores in Sydney.<sup>136</sup> The study finds that although ready to drink (RTD) sales fell by 44%, spirits sales rose by 21%, wine cask sales rose 16%, cider sales rose 17%, and a type of wine-based RTD, which was exempt from the tax, rose 71%.<sup>137</sup> With the presence of these statistics as well as another survey demonstrating that substitution occurred, Independent Distillers Australia doubts the likelihood of the tax achieving its public health goals if drinkers are simply switching to straight spirits.<sup>138</sup>

Independent Distillers Australia also criticizes the forward revenue estimates. Although RTD consumption is supposed to decrease, the government expects the revenue from the excise tax on alcopops to increase annually.<sup>139</sup> Specifically, the model utilized by the Treasury Department suggests that tax revenues will grow faster than inflation, despite predicting a 4% decrease in RTD consumption.<sup>140</sup> Given the data from Chambers Cellars, the Treasury’s data could be overestimated by 40%.<sup>141</sup> Independent Distillers Australia points to the Treasury Department’s admissions as a “silver bullet”:

The relatively new existence of RTDs within the market place makes it difficult to determine precisely the sensitivity of the volume sales of RTDs relative to changes in their prices. Conceptually, changing the price of RTDs can have two effects. The first is an own price elasticity which is the change in the consumption of RTDs due to the change in the price of RTDs. The second possibility is a re-direction of alcohol

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<sup>134</sup> *Id.* at 4.

<sup>135</sup> *Id.*

<sup>136</sup> *See id.* at 5 (studying and comparing a four-week period after the tax was put in place 2008 and the corresponding four weeks in 2007).

<sup>137</sup> *Id.*

<sup>138</sup> *See id.* at 13 (finding that 63% of RTD drinkers have changed their preferred drink in response to the excise tax, including 47.3% of female and 51% of male RTD drinkers switching to spirits, and 67% of underage RTD drinkers switching to spirits).

<sup>139</sup> *Id.* at 4, 14.

<sup>140</sup> *Id.* at 15.

<sup>141</sup> *Id.*

consumption to other products as a result of the change in price of RTDs.<sup>142</sup>

After noting the importance of the substitution effect and the problem with the Treasury numbers, Independent Distillers Australia makes the extremely important point that there is more than just economics involved in an individual's decision to purchase alcohol.<sup>143</sup> They acknowledge that social and cultural norms play an enormous role in alcohol consumption, and an approach relying solely on a price increase to lower consumption of one type of alcohol will fail to achieve meaningful results.<sup>144</sup>

Taking these two submissions into consideration, the Standing Committee on Community Affairs generally supported the proposed tax increase and recommended further measures to approach the issue.<sup>145</sup> The Committee found enough evidence supporting the tax and found the substitution effect to be minimal.<sup>146</sup>

The events occurring in Australia during the twelve-months following the implementation of the original tax did not confirm the optimistic view of the Senate Committee report; the legislation was lambasted for being a blatant tax grab by the opposition, and the substitution effect was publicized and corroborated by the industry.<sup>147</sup> When the eventual vote in the Senate arrived on March 19th, the tax was narrowly defeated by a vote of 32-to-31.<sup>148</sup> The single deciding vote was a Member of Parliament not aligned with either major party, but rather a member looking to trade his decisive vote for a pledge by the majority party to ban alcohol company sponsorship

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<sup>142</sup> *Id.*

<sup>143</sup> *Id.* at 16.

<sup>144</sup> *Id.*

<sup>145</sup> DISTILLED SPIRITS INDUS. COUNCIL OF AUSTL., *supra* note 33, at 42–43.

<sup>146</sup> *Id.*

<sup>147</sup> See Bridie Smith, *Alcopops Sales Down, but Spirits Booming*, AGE (July 28, 2008), <http://www.theage.com.au/national/alcopops-sales-down-but-spirits-booming-20080727-3lqe.html> (reporting that data to be released from the Liquor Merchant's Association of Australia shows a 30% decrease in the volume of RTD products sold, but a 46% rise in the volume of full strength spirits sold over that same time, as well as reports from Southern Independent Liquor Group of a 20% increase in the sale of bottled spirits); see also Siobhain Ryan, *Alcopop Drinkers 'Turning to Spirits'*, AUSTRALIAN (May 29, 2008), <http://www.theaustralian.com.au/news/nation/alcopop-drinkers-turning-to-spirits/story-e6frg6nf-111116473776> (quoting the Distilled Spirits Industry Council of Australia's research manager, Stephen Riden, in reporting that one company has reported an 85% increase in full spirit sales along with a 30% decrease in alcopop sales); see also Franklin, *supra* note 13 (discussing the plan of the opposition in the Australian Senate to block the alcopop tax legislation).

<sup>148</sup> Daniel Palmer, *Alcopop Tax Fails to Clear Final Hurdle*, AUSTRALIAN FOOD NEWS (Mar. 19, 2009), <http://www.ausfoodnews.com.au/2009/03/19/alcopops-tax-fails-to-clear-final-hurdle.html>.

at sporting events.<sup>149</sup> Senator Stephen Fielding did not get his deal with the majority and voted along with the opposing party and the rest of those opposing the bill.<sup>150</sup> The immediate legal question was the return of the tax revenue to the distillers, but the industry has maintained its view that the revenue should instead be put toward alcohol education.<sup>151</sup> In May 2009, two bills were passed without objection, allowing the government to retain the original tax proceeds.<sup>152</sup>

On the second legislative attempt, the Rudd government achieved success, passing the bill with an overwhelming majority of the votes in the Senate.<sup>153</sup> Many in the opposition still clearly expressed their disapproval for the bill since it was a “tax grab,” but ultimately their last minute dealings with the Rudd government held strong.<sup>154</sup> While there is little information as to why the opposition went along with the second coming of the alcopops tax, the looming possibility of a “double dissolution election”<sup>155</sup> could have played a part.<sup>156</sup> It is also possible that the opposition may have simply caved to the proposition of facing an election earlier than expected.

In the aftermath of the eventual tax hike, some in the industry reported double-digit growth in the alcopop market.<sup>157</sup> The industry has forged on with production of RTD lines as they have relied on customers eventually returning to the convenience of the product.<sup>158</sup>

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<sup>149</sup> Jennifer Doggett, *Alcopops Defeat a Win for Distillers*, ABC NEWS (Mar. 20, 2009), <http://www.abc.net.au/news/stories/2009/03/20/2521963.htm>.

<sup>150</sup> *Id.*

<sup>151</sup> See *Distillers to Donate Alcopop Tax Refund*, SYDNEY MORNING HERALD (Mar. 19, 2009), <http://news.smh.com.au/breaking-news-national/distillers-to-donate-alcopop-tax-refund-20090319-92gl.html> (declaring that distillers have promised to contribute any tax refund to health advocacy groups and increasing naming labels).

<sup>152</sup> *Senate Vote Will Allow Government to Keep Extra Alcopop Tax Takings*, SYDNEY MORNING HERALD (May 12, 2009), <http://www.smh.com.au/business/federal-budget/senate-vote-will-allow-government-to-keep-extra-alcopop-tax-takings-20090512-b1hk.html>; Summary of Alterations, *supra* note 112.

<sup>153</sup> Katharine Murphy, *Alcopops Tax into Law, Opposition in Disarray*, AGE (Aug. 14, 2009), <http://www.theage.com.au/national/alcopops-tax-into-law-opposition-in-disarray-20090813-ejve.html>.

<sup>154</sup> *Id.*

<sup>155</sup> This procedure is provided for in the Australian Constitution as a means of resolving deadlock and permits the Governor-General to dissolve the House and Senate and issue writs of election for every seat. AUSTRALIAN CONSTITUTION s 57.

<sup>156</sup> Matthew Franklin & Siobhain Ryan, *Alcopops May Trigger Double Dissolution*, AUSTRALIAN (Apr. 16, 2009), <http://www.theaustralian.com.au/news/nation/alcopops-may-cause-double-dissolution/story-e6frg6nf-1225699219840>.

<sup>157</sup> Christain Kerr & Matthew Franklin, *Alcopops Still Flow Despite Tax Rise*, AUSTRALIAN (Nov. 7, 2009), <http://www.theaustralian.com.au/business/industry-sectors/alcopops-still-flow-despite-tax-rise/story-e6frg98o-1225795200239>.

<sup>158</sup> Eli Greenblat, *Bacardi Lion Breezily Shrugs Off Alcopops Tax*, SYDNEY MORNING HERALD (Nov. 23, 2009), <http://www.smh.com.au/business/bacardi-lion-breezily-shrugs-off-alcopops-tax-20091122-issz.html>.

*B. The Law in the United States*

Alcopop taxation in the United States is very different and much more complex than it is in Australia because states are authorized to develop their own regulatory schemes and tax structures.<sup>159</sup> This power is granted to the states by the Twenty-first Amendment,<sup>160</sup> which provides state government the independent authority and responsibility to classify alcohol products.<sup>161</sup> This is in stark contrast to the Australian model for taxation of alcohol, where only one taxing authority on alcohol exists at the federal level.<sup>162</sup>

The Marin Institute is the only organization that attempts to track alcopops tax legislation on a national scale and published an updated survey of the nation in October 2009.<sup>163</sup> A majority of states have not yet addressed the issue and continue to tax alcopops as beer.<sup>164</sup> It is also worth noting the two most extreme views espoused in the United States. The first view addresses states that have made the shift to tax alcopops as distilled spirits and the second addresses those that have adopted the Federal Alcohol and Tobacco Trade and Tax Bureau definition.<sup>165</sup> Each view is addressed in more depth later in the Note.

As of 2009, three states had passed legislation to classify alcopops as distilled spirits for tax purposes: California, Maine, and Utah.<sup>166</sup> In 2005, Maine was the first state to effect a change in its law.<sup>167</sup> Maine did not create a new class of beverages or license, but rather reclassified alcopops into their existing "low-alcohol spirits" category.<sup>168</sup> As a result, alcopops could only

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<sup>159</sup> James F. Mosher, *Litigation and Alcohol Policy: Lessons from the US Tobacco Wars*, 104 ADDICTION 27, 30 (2009). The federal government is involved in the taxation, production, and advertising of alcohol, but the current battleground for the alcopops tax is the states. In 2005, the TTB decided how to tax alcopops at the federal level. *Id.*

<sup>160</sup> U.S. CONST. amend. XXI.

<sup>161</sup> JAMES F. MOSHER, STATUS OF CAMPAIGNS TO RESTRICT THE AVAILABILITY OF ALCOPOPS 2 (2009), available at [http://www.alcoholpolicyconsultations.com/downloads/Alcopop\\_status\\_report\\_2-09-09.pdf](http://www.alcoholpolicyconsultations.com/downloads/Alcopop_status_report_2-09-09.pdf). The practical result of this setup is of course fifty different classification battles. *Id.*

<sup>162</sup> See AUSTRALIAN CONSTITUTION s 90, available at [http://www.comlaw.gov.au/comlaw/legislateon/ActCompilation1.nsf/0/9E74CC7B0879A06060CA25771C001E95E7/\\$\\$file/Constitution\\_WD02.pdf](http://www.comlaw.gov.au/comlaw/legislateon/ActCompilation1.nsf/0/9E74CC7B0879A06060CA25771C001E95E7/$$file/Constitution_WD02.pdf) (declaring that only Parliament may impose "duties of customs and of excise, and to grant bounties on the production or export of goods, shall become exclusive").

<sup>163</sup> *State by State Analysis of Alcopops Law*, MARIN INST. (Oct. 19, 2009), [http://www.marininstitute.org/site/index.php?option=com\\_content&view=article&id=319:state-by-state-analysis-of-alcopops-law&catid=6&Itemid=6](http://www.marininstitute.org/site/index.php?option=com_content&view=article&id=319:state-by-state-analysis-of-alcopops-law&catid=6&Itemid=6) [hereinafter *State Analysis*].

<sup>164</sup> *Id.*

<sup>165</sup> *Id.*

<sup>166</sup> *States Where Alcopops Are Properly Classified as Distilled Spirits*, MARIN INST. (Oct. 5, 2009), <http://www.marininstitute.org/site/component/content/article/6-stop-alcopops/320-states-where-alcopops-are-properly-classified-as-distilled-spirits.html> [hereinafter *Distilled Spirits*].

<sup>167</sup> *Id.*

<sup>168</sup> Letter from Jessica L. Maurer, Special Assistant Attorney Gen. to James F. Mosher, Ctr.

be sold in locations possessing wine permits and faced a tax of \$1.54 per gallon, an increase from the previous rate of \$.35 per gallon when classified as beer.<sup>169</sup> It is noteworthy that because it was only a “reclassification,” the change was achieved by an administrative ruling from the Department of Public Safety, instead of through legislation.<sup>170</sup>

Utah followed suit in 2008, but its path was slightly different. In 2007, the Utah Alcohol Beverage Control Commission first issued a unanimous decision classifying alcopops as distilled spirits.<sup>171</sup> The Commission sought legislative review and in 2008, Senate Bill 211 was passed.<sup>172</sup> In addition to the tax changes, the bill required alcopops to be sold only in liquor stores and included new labeling requirements that would clearly indicate that the beverages contain alcohol.<sup>173</sup>

The most publicized and controversial battle to reclassify alcopops took place in California. In 2005, the Attorney General wrote a letter to the Board of Equalization concluding that alcopops should be classified for tax purposes as “distilled spirits.”<sup>174</sup> In response, the alcopop industry lobbied for Assembly Bill 417, which would have defined alcopops as beer for taxation purposes.<sup>175</sup> Although the Assembly passed the bill, the Governor vetoed it.<sup>176</sup> In 2008, the California Board of Equalization finally voted to increase the tax rates on alcopops from \$.20 per gallon to \$3.30 per gallon.<sup>177</sup> However, the new regulations exempted alcopops that obtained less than 50% of its alcohol content from added distilled spirits, thus excepting some traditional beers that contained trace amounts of distilled spirits flavoring.<sup>178</sup> Therefore, virtually all alcopops in California purportedly meet this new 50% standard.<sup>179</sup>

As of 2009, seven states have passed legislation to classify alcopops as beer for taxation purposes: Maryland, Minnesota, Missouri, Oregon,

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for the Study of Law and Enforcement Pol’y Director (Aug. 1, 2007), *available at* [http://www.marininstitute.org/site/images/stories/pdfs/maine\\_%20alcopop\\_letter.pdf](http://www.marininstitute.org/site/images/stories/pdfs/maine_%20alcopop_letter.pdf).

<sup>169</sup> *Distilled Spirits*, *supra* note 166.

<sup>170</sup> Maurer, *supra* note 168.

<sup>171</sup> *Distilled Spirits*, *supra* note 166.

<sup>172</sup> UTAH CODE ANN. § 32A-1-801 (2010).

<sup>173</sup> *Id.*

<sup>174</sup> Letter from Bill Lockyer, Cal. Attorney Gen. to Dennis Maciel, Excise Taxes and Fees Div. Chief (May 24, 2005), *available at* [http://www.marininstitute.org/site/images/stories/pdfs/california\\_attorney\\_general\\_to\\_boe\\_05.pdf](http://www.marininstitute.org/site/images/stories/pdfs/california_attorney_general_to_boe_05.pdf).

<sup>175</sup> MOSHER, *supra* note 161, at 3–5.

<sup>176</sup> *Id.*

<sup>177</sup> Press Release, Cal. Bd. of Equalization, Judy Chu Announces Flavored Malt Beverages to be Taxed As Distilled Spirits (June 11, 2008), *available at* <http://www.boe.ca.gov/news/2008/37-08-C.pdf>.

<sup>178</sup> MOSHER, *supra* note 161, at 3–5.

<sup>179</sup> *Id.*

Tennessee, Virginia, and Washington.<sup>180</sup> All of these states have essentially adopted the TTB's ruling that alcopops containing no more than 49% of their alcohol from distilled spirits would be classified as "beer."<sup>181</sup> Maryland was a particularly intense battleground as the Attorney General admonished the legislature that classifying alcopops as "beer" was "bad public policy."<sup>182</sup> Maryland House Bill 745 passed and under pressure from both sides, the Governor of Maryland opted to neither sign nor veto the bill, allowing it to pass.<sup>183</sup> Maryland law classifies alcopops as "beer" if it contains less than 6% alcohol by volume and the alcohol is derived primarily from the fermentation of grain with less than 49% of the alcohol obtained from added distilled spirits.<sup>184</sup>

## V. ANALYSIS

The question of alcopop regulation can be simplified by examining two basic questions. First, what is the proper classification of alcopops? Second, does increased taxation and placement regulation in order to protect youth actually work?

### A. *The Classification of Alcopops*

The federal governments in both Australia and the United States have reached different conclusions about the classification of alcopops. The United States has adopted the 49% standard and many states have followed,<sup>185</sup> while Australia has chosen to target alcopops directly and increase the tax on them by 70%.<sup>186</sup> The two countries seem to have had different impetuses in reaching their respective decisions. Australia took a broad, public policy approach through its national legislature, while the United States took a code-based and insular approach through the TTB. This dichotomy made all the difference. It is improper to say if one approach of the two is correct in its classification of alcopops. Australia did not place

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<sup>180</sup> *State Analysis*, *supra* note 163.

<sup>181</sup> *States Where Industry Got Laws Changed to Undermine Public Health*, MARIN INST. (Oct. 5, 2009), available at [http://www.marininstitute.org/site/index.php?option=com\\_content&view=article&id=322:states-where-industry-had-laws-changed-to-undermine-public-health&catid=6&Itemid=6](http://www.marininstitute.org/site/index.php?option=com_content&view=article&id=322:states-where-industry-had-laws-changed-to-undermine-public-health&catid=6&Itemid=6).

<sup>182</sup> *Id.* at 9.

<sup>183</sup> *Md. Gov. Won't Veto Alcopop Bill*, PARTNERSHIP AT DRUGFREE.ORG (May 23, 2008), <http://www.drugfree.org/join-together/alcohol/md-gov-wont-veto-alcopop>.

<sup>184</sup> MD. CODE ANN., *Alcoholic Beverage Tax* § 5-101 (West 2010).

<sup>185</sup> JAMES MOSHER, THE CDM GROUP, INC., *STATUS OF STATE CAMPAIGNS TO RESTRICT THE AVAILABILITY OF ALCOPOPS 1* (2009), available at [http://www.alcoholpolicyconsultations.com/downloads/Alcopop\\_status\\_report\\_2-09-09.pdf](http://www.alcoholpolicyconsultations.com/downloads/Alcopop_status_report_2-09-09.pdf).

<sup>186</sup> Gordon & Harrison, *supra* note 114.

alcopops into a specific category so much as it simply made a public policy decision to tax alcopops at a higher rate. If the United States took a legislative approach to this issue, this may well have been the outcome. However, Americans do not consume alcopops at a rate even close to the rate at which Australians do.<sup>187</sup> Consequently, the concern over youth consumption and abuse of alcopops is obviously less in America. For this reason, the national outcry to correct the problem has not been as publicized in the United States.

This basic difference in motivation for each country takes the focus off of the first question for Australia—its legislature has created new law classifying alcopops. The question of classification is now one of effectiveness. For the United States, though, where many states make the decision within regulatory bodies, the issue looms. The characteristics of alcopops allowing it to float somewhere between beer and distilled spirits, were undoubtedly the intention of the design. The industry saw the opportunity for a classification of a lighter beer style beverage with the characteristics of a mixed liquor drink. In order to be sold and advertised as beer, the drink had to have lower alcohol content than a typical distilled spirit and be produced by fermentation,<sup>188</sup> and Alcopops passed this initial test. The question now is, whether the alcopops industry is taking advantage of the regulations.

In answering that question, the basic issue of differing taxation for beer and distilled spirits is invoked. Beer is produced by fermentation and liquor by distillation.<sup>189</sup> The end product is a difference in alcohol content by volume, which along with social factors, must be the reasoning for discrepancy in regulation and taxation. Therefore, if the basic approach were to tax solely upon alcohol by volume, and if alcopops fit in the standard range of beer, one would assume they should be taxed as beer. The TTB, however, has found that the traditional delineation is based upon whether a beverage derives the majority of its alcohol through fermentation or distillation.<sup>190</sup> Therefore, the type of alcohol, and not the amount, is the relevant characteristic. This argument makes sense to some degree because, by volume, distilled spirits have higher alcohol content. It is an arbitrary distinction to make, however, when the alcohol by volume is identical. With the current definition and without altering the brewing process, the majority

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<sup>187</sup> Australian Drug Foundation, *supra* note 119.

<sup>188</sup> See VT. DEP'T OF LIQUOR CONTROL, *supra* note 2 (stating that the definition of "beer" does not typically include a product that derives most of its alcohol content from distilled spirits).

<sup>189</sup> 27 C.F.R. § 7.11 (2005).

<sup>190</sup> *Id.*

of alcopops would not be classified as "beer," although the industry apparently is able to adapt and meet this new definition.

The option that would make the most sense is to get rid of the beer/distilled spirits delineation, and tax solely based upon alcohol content. The alcohol content percentage could also provide a useful mechanism for deciding where particular types of alcohol could be sold. For instance, anything above 6% alcohol content would be required to be sold in liquor stores and anything below could be sold in the grocery stores, gas stations, and other similar facilities.

Alcopops do not fit into the traditional conception of beer, but if they have similar alcohol content and derive a majority of their alcohol through fermentation, then classifying them similar to beer may be appropriate. A basic rate on all alcohol makes more sense than a classification based upon distillation or fermentation, while eliminating the guesswork in hybrid products. Such an approach is obviously not acceptable to those lobbying for classification of alcopops as distilled spirits. Their position in the debate is motivated not by the desire to find an answer to the classification inquiry but rather to limit its availability to youth.<sup>191</sup>

#### *B. The Protection of Youth and Alcopop Classification*

Beyond the question of how and why types of alcohol are classified for taxation and regulation purposes is the issue of controlling alcopops as a means of protecting underage youth from alcohol consumption and abuse. The regulation of alcopops as distilled spirits is generally utilized as a tool to decrease consumption and limit availability, depending on the jurisdiction.

The question of how best to curb youth consumption turns on effectiveness of these methods. Does increasing the price of a singular alcohol product decrease consumption of that product specifically and others? Given the discussion in this Note, the answer appears to depend on trusting the statistics of the alcohol industry or the public health coalition, both of which have an agenda they are pursuing. On a practical level, one cannot discount the likelihood of the substitution effect. Predicting what teenagers will do is not a simple economic choice problem, as teenagers are subject to peer pressure, fads, trends, and prevailing social norms. If it is the desire of youth to consume alcohol, simply raising the price of a favorable product will not truly address the issue. The extra money will be spent on the same product, or they will simply find a cheaper substitute beverage.

This concern has not stopped Australia and some states in the U.S. from attempting to increase the tax on alcopops, but it is still too early to gauge

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<sup>191</sup> *Md. Gov. Won't Veto Alcopop Bill*, *supra* note 183.



their true effectiveness. It is clear from the history of this type of legislation in the United States and Australia that passage will be hotly contested and lobbied against by the alcopop industry. Even in a state where the public health coalition claims success, such as California, the alcopop industry is still evading the tax via the 50% exception. While Australia has solidified a tax on alcopops in perpetuity,<sup>192</sup> U.S. states appear unwilling to adopt the TTB recommendations. For example, even in the worst of economic times, only two states have implemented an effective tax<sup>193</sup> and many more have passed legislation that defines alcopops as beer.<sup>194</sup> State budgets may be hurting, but legislators also have campaign funding concerns. As previously noted, there was only one battle to fight in Australia, as opposed to fifty separate campaigns that would have to be waged in the United States. Further, Australia faces a more serious alcopop or alcohol crisis than the United States.

Even if many states ultimately pass legislation similar to that of Australia, both sides of the debate would agree that it would not be enough to curb underage drinking. Education and a fundamental societal shift seem to be the only way to fully address the issue. Increased alcohol taxes could certainly be a part of that solution, but alone they are not likely to lead to significant change.

## VI. CONCLUSION

One thing is for certain: the alcopop tax alone is not enough to lead to any real change. The movement in Australia and the eventual passage of the tax was bloodied by claims of being a blatant tax grab and fundamentally unsound. It passed as the pet legislation of an administration that pulled out all the stops to achieve success. Perhaps the tax would have been a greater success if it were not made the mantelpiece of Prime Minister Rudd's plan to combat drinking. The tax became a political football, however, and its eventual passage was not accompanied by implementation of further plans to effect real change.

A similar scenario within the United States is unlikely due to the structural differences and the lack of a clear movement to curb underage drinking as a policy. Even where it was promoted as a national issue in Australia, the alcopop industry was barely victorious. This is not to say that at some point in the United States, the societal effect of alcohol consumption will be made an issue and taxes will become an issue at every level.

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<sup>192</sup> Gordon & Harrison, *supra* note 114.

<sup>193</sup> *Distilled Spirits*, *supra* note 166.

<sup>194</sup> MOSHER, *supra* note 161.

Currently, however, even in the present budget crunch, the alcopop industry is winning the state-by-state battle.