

U.S. Senate Committee on Finance

MEMORANDUM

To: Reporters and Editors
Re: Manufacturing tax relief and eligibility
Da: Tuesday, Oct. 26, 2004

A Bloomberg article this week incorrectly asserts that the Starbucks Corp. will get manufacturing tax relief for brewing coffee under the newly enacted business tax law. Sen. Chuck Grassley, chairman of the Committee on Finance, and Sen. Max Baucus, ranking member, today made the following comment on this.

“The article contains a point that is factually and legally incorrect. The bill does not treat coffee brewing as manufacturing. Food preparation at restaurants is specifically excluded from manufacturing. The example in the conference report is meant to draw a distinction between the roasting of coffee beans, which qualifies for the manufacturing tax break, and the brewing of coffee, which does not. The suggestion that brewing a vanilla latte constitutes manufacturing demonstrates a fundamental misunderstanding of the conference report.

“The coffee roasting example simply illustrates that the manufacturing rate cut is neutral regarding a manufacturer’s choice of distribution channels. For example, computer manufacturers may sell to customers over the Internet, through third-party retailers, or in their own retail stores. The manufacturing tax break does not discriminate against any of these choices. In the coffee roasting example, sales of the company’s roasted beans in a company-owned store are treated no differently than sales of beans to an unrelated coffee shop. To the extent a company’s beans are used in brewing its coffee, the profits attributable to roasting those beans would qualify for the manufacturing rate cut, but the profits attributable to brewing the latte and serving it in the retail store would not. This ensures that the company is not prejudiced for using its own beans rather than selling them to a competitor. The conference report specifically states that profits from brewing coffee do not qualify as manufacturing.

“The article’s implication that Starbucks received special treatment under the bill is misplaced. The specific example in the conference report was necessary to clarify that the food services exception does not taint all of the ‘upstream’ manufacturing activity of a vertically integrated manufacturer. A vertically integrated manufacturer may own part or all of its raw materials sources, the factory, and the retail stores for selling its manufactured product. This is not a common ownership structure for most American manufacturers, the majority of which buy raw materials from multiple sources and sell their products to various unrelated retailers.

“The article’s implication that coffee bean roasting is a new manufacturing activity invented under the bill is also erroneous. According to Starbucks, it would have been eligible for extraterritorial income benefits for beans that it roasted in America and exported to its foreign retail stores.”