WINE TASMANIA

SUBMISSION TO THE AUSTRALIAN GOVERNMENT'S WINE EQUALISATION TAX REBATE: TIGHTENED ELIGIBILITY CRITERIA IMPLEMENTATION PAPER

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Introduction

The Tasmanian wine sector is an important and growing contributor to trade and the economy, regional employment, tourism and the overall Tasmanian brand. Driven by a clear, market-led strategy, the Tasmanian wine sector is:

- Gaining a global reputation for the quality of its wines, including through international wine shows and independent endorsements;
- Encouraging strong visitation to Tasmania and its cellar doors, with wine being one of the top three motivations for visitors and one in five of all visitors calling into a cellar door (233,000+ over the past twelve months, an increase of 12% on the previous year);
- Growing its investment in regional communities, through new vineyard plantings, processing facilities, cellar door / tourism developments and other infrastructure - Tasmania is bucking the national trend in production growth, with the most recent Vineyard Census reporting that overall yield decreased by 11% in the cool and temperate regions of Australia in 2012/13, in contrast to Tasmania's growth of 14% over the same period; and
- Attracting new investment, with significant investments over the past 5-6 years by Hill Smith Family Vineyards, Brown Brothers, Shaw + Smith and Treasury Wine Estates, as well as many individuals moving to Tasmania from elsewhere to be part of growing grapes and making wine in Tasmania.

The island's wine producers exclusively operate within the niche, high premium Australian wine offering above the retail equivalent of $15 per bottle. This segment represents just 7% of Australia's total wine production but generates 28% of its value[1].

Tasmania's wine sector has developed a strong, clear and collaborative position in the wine world, built on quality and value. Contrary to many other Australian wine regions, demand for Tasmanian wine continues to outstrip supply, and strong growth is occurring in the Tasmanian wine sector.

This growth is occurring in spite of many challenges, including low economies of scale, higher costs of production, including those associated with a longer ripening period and hand harvesting / pruning, freight, significant vintage variability due to our cooler climate, as well as a taxation system that is based on value, disproportionately impacting on high value wine producers.

[1] *Winemakers' Federation of Australia Expert Review, Centaurus Partners*

The Government's recent proposals to change wine tax would have the impact of increasing net taxes paid by Tasmanian wine producers. Of most concern is the threat to Tasmania's significant rates of growth, which would most likely be arrested.

Wine Tasmania appreciates the opportunity to provide input on proposed changes to eligibility through this formal implementation paper, and notes that this paper does not specifically seek input on the critical issue of a proposed reduction in the rebate. This is particularly important, given the impact this would have on Tasmania's small, high value wine producers. Within Tasmania, the rebate is being utilised as was originally intended, to support small wine producers and the regional economies to which they contribute.

1. The Federal Budget announcement included a proposed reduction in the Wine Equalisation Tax rebate from the current $500,000, to $350,000 from 1 July 2017 and to $290,000 from 1 July 2018
   Wine Tasmania rejects the proposal to reduce the Wine Equalisation Tax rebate.

2. The Federal Budget announcement proposed changes to the criteria for wine producers and wine that would be eligible for the rebate, effective 1 July 2019
   Wine Tasmania supports changes to the criteria for wine producers and wine to be focused on branded wine owned by wine producers and implementation of revised eligibility criteria earlier than the proposed timeframe of 1 July 2019.

Further comments regarding proposed changes to eligibility and specific questions posed in the implementation paper follow.

Wine Tasmania reaffirms its position, stated throughout previous submissions on wine taxation, that removal or reduction of the WET rebate cannot be considered separately to the overall structure of wine tax.

Snapshot of Tasmania's Wine Sector[2]

- 1,410 full time equivalent positions
- 160 licensed wine producers
- 200+ vineyards covering 1,880 hectares
- Average annual production of 625,000 dozen, less than 1% of national production
- 90 cellar door outlets, with 233,000+ tourists visiting wineries - 20% of all visitors (2016)
- Key varieties - Pinot Noir 41%, Chardonnay 18%, Sauvignon Blanc 17%, Pinot Gris 10%, Riesling 8%
- Sparkling wine production - 35% of total production (76% of Chardonnay and 45% of Pinot Noir)
- Sales percentages (approximate) - Tasmanian 40%, mainland Australia 54%, export 6%
- Highest pricing for Pinot Noir, Chardonnay, Riesling and Sauvignon Blanc grapes in Australia
- Average bottle value of $22.36, compared with the national average of $10.87 per bottle
- The value of Tasmanian wine sales is growing at almost double the Australian wine sales value

Wine Tasmania Overview

Wine Tasmania is the peak representative body for Tasmanian grape growers and winemakers, working to assist them to be recognised as world leaders in the sustainable production of premium cool climate wine.

Established in 2006 as a public company limited by guarantee, the Wine Tasmania Board is skills based and chaired by independent director Graeme Lynch. Other directors are Will Adkins (Brown Brothers), Jeremy Dineen (Josef Chromy Wines), Rebecca Duffy (Holm Oak Vineyards), Scott Dawkins (independent), Anna Pooley (Pooley Wines) and Guy Taylor (independent).

Wine Tasmania represents more than 98% of Tasmanian wine production, with around 100 state-wide producer members and 50 associated member businesses, and operates against a clear Strategic Plan, which is available at www.winetasmania.com.au and focuses on the following key themes:

1. The current highly competitive global market demands a differentiated and collegiate approach by Tasmanian wine producers.
2. The profitability, productivity and performance of Tasmanian vineyards and wine businesses need to be improved to build global competitiveness.

[2] *Sources: Tourism Tasmania Visitor Statistics, Wine Tasmania Vintage Reports, Wine Australia Winegrape Dispersion Report, Winemakers' Federation of Australia Vintage Report, Gaetjens Langley, Nielsen*

3. In order to meet the challenges of a highly competitive market, Tasmanian wine producers need to increase and encourage visitation and sales through a differentiated offering at their cellar doors and vineyards.
4. Small to medium sized, time-constrained wine producers require support to evolve their business capabilities.

Comments on the Australian Government's Proposed Changes to Wine Tax

Wine Tasmania supports the Government's announcement that it will "address integrity concerns with the WET rebate and better target support to small wine producers in rural and regional Australia". Wine Tasmania believes that this aim can be supported through tightened eligibility criteria and an increase in compliance / anti-avoidance measures.

Wine Tasmania does not believe that the rebate should be reduced, but rather more directly targeted at small wine producers in rural and regional Australia through tightened eligibility and compliance measures.

In Tasmania, the rebate is being utilised as was originally intended, to support small wine producers and the regional economies to which they contribute. The WET rebate is supporting smaller producers as they continue to grow and reinvest in their businesses.

Wine Tasmania recognises that the rebate has evolved beyond its original intent and is therefore contributing to distortions in the wine sector. Specifically, this relates to the following:

1) The ability of brokers, intermediaries and uncommercial arrangements to access the entitlement;
2) The role of the rebate in delaying the correction to the supply/demand imbalance by underpinning the conversion of uncommercial grapes into bulk wine and ultimately low equity cleanskins and home brands; and
3) The ability of New Zealand entities to access the entitlement on unfair and preferential terms.

Wine Tasmania supports reforms being made to the rebate to remove these distortions and return the rebate to its original intent of supporting regional producers, <u>without reducing the rebate</u>, and supports the earlier implementation of agreed changes to the definition of rebatable wine and eligible producers.

It is important to recognise the origins of the rebate, in particular the fact that it replaced the state-administered cellar door subsidy program, which supported regional wine producers. Proposals to remove the rebate ignore these origins and the importance of contributions by wine producers to the many regional communities around Australia.

Reforming and returning the WET rebate to its original intent through tightened eligibility and compliance measures would also support the Australian wine sector's market-led approach to improve the sector's performance through promotion of our fine, branded wines.

In the current value-based tax structure, Tasmania's wine producers are among the highest taxed, and it is only the rebate that provides a counterbalance and has allowed the sector to continue to grow its contribution to the state's economy. This is in the context of the rebate being applied in line with its original intent in Tasmania - recognising and supporting small wine producers contributing to regional economies.

Whilst the Tasmanian wine sector is in a strong position, Tasmania is an expensive place to grow grapes and make wine. It is difficult for producers to recover these high costs in a highly competitive marketplace, where there is constant pressure on pricing. Wine Tasmania rejects any proposals that would result in increases the net taxes paid by Tasmanian wine producers.

Response to WET Rebate: Tightened Eligibility Implementation Paper

In the context of the comments above, Wine Tasmania provides the following responses to the specific implementation paper questions, and appreciates the opportunity for ongoing input and consultation on changes and the potential timing of these changes.

Question 1: For rebatable wine, is the proposed definition of packaged and branded wine appropriate? If a trade mark approach is used, what types of trademarks should be permitted and what would be the impact?

Wine Tasmania supports the rebate applying only to branded wine, not to bulk or unbranded, and supports this being through a registered or common law trademark, owned by a wine producer (not licensed), packaged in containers up to 5L.

Wine Tasmania notes the opportunity for national harmonisation of licensing, which could include a consistent license for wine producers and be utilised in the administration of the rebate. Whilst not directly related, this would also assist wine producers who currently need to undertake training and receive certification for responsible service of alcohol requirements on a state by state basis.

Question 2: For eligible producers, how should a winery ownership and leasing test be applied? What should be the nature and extent of investment in the wine industry required to access the rebate and how can this be implemented?

It is inappropriate for the rebate to be restricted to winery ownership or leasing only. Within Tasmania and around Australia, there are many varied, and valid, wine business models in operation.

One of the most common models is for a wine business to own / operate a vineyard and have their own branded wine made under contract. Within Tasmania, the conservative costs to manage a vineyard (not including land or establishment costs) are approximately $15,000 per hectare.

Not only are the costs very high, vineyard owners and managers in Tasmania face significant risks posed by the island's cool climate, with annual production varying by as much as 50% due to climatic conditions. Further information on the costs of operating a vineyard in Tasmania can be provided, but there is absolutely no question that the commitment of owning / operating a vineyard in Tasmania is at least an equal commitment to that of owning / operating a winery.

Wine Tasmania supports the national wine sector's view that changes to the rebate eligibility should be with the key outcome of removing the rebate from bulk and unbranded wines.

The further proposal outlined in the implementation paper regarding ownership of grapes from the crusher and throughout the winemaking process has merit, although wine producers should not be penalised for securing wine from previous vintages that may become available to supplement their own wine grape production, particularly given the significant vintage variability of Tasmanian production. In this context, Wine Tasmania supports a requirement for 85% of grapes to be owned at the crusher and through to branded wine, fit for retail sale.

Wine Tasmania does not agree that an 'asset test' is necessary.

Question 3: What is the impact from a 1 July 2019 start date of the tightened eligibility criteria? How might this change from an earlier transition period?

In the interests of improving the rebate integrity and subject to agreement on the tightened eligibility criteria, Wine Tasmania supports its introduction earlier than the 1 July 2019 date proposed.

Modelling by Price Waterhouse Coopers, commission by the Winemakers' Federation of Australia, indicates that there is revenue to be generated of approximately $200M over four years as a result of removing the rebate from bulk and unbranded wine through tightened eligibility criteria.

Wine Tasmania supports the earlier introduction of agreed eligibility criteria, and highlights the opportunity to utilise this additional revenue to retain the rebate at its current cap of $500,000 and its partial application towards additional support for wine marketing and tourism initiatives.

Conclusion

Wine Tasmania believes that the overall Australian wine sector and its global performance can benefit from a significantly increased focus on the country's high quality wine. With such a high proportion of the country's wine production being reported as unprofitable[3], it is clear that the overall value of the sector needs to increase.

The clear, long term strategy taken by Wine Tasmania is to focus on the high quality and value offering of its wines. To date, this has been successful in growing the global awareness and value of Tasmanian wines, although there is still significant opportunity to grow our markets and value.

Australia is not able, nor should necessarily want, to be the cheapest wine producer in the world, and therefore needs to focus on promoting its strengths and unique attributes. It is Wine Tasmania's view that a focus on high quality / fine wines should translate through to all aspects of the wine sector's operations, including a strategic, long term and consultative marketing strategy and activities as well as allocation of research, development and extension resources.

The proposed reforms to the rebate eligibility would support this objective by focusing on smaller, regional, branded wine producers. The proposed reduction in the rebate does not support this objective, given the disproportionate impact it will have a small, regional, branded wine producers, particularly high value producers such as those in Tasmania.

[3] *Winemakers' Federation of Australia Vintage Report and Production Profitability Analysis*