**SUBMISSION – RE:THINK**

**DISCUSSION PAPER**

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Authors: CCW Co-operative Limited

PO Box 238 Berri

SA 5343

This submission is prepared by CCW Co-operative Limited on behalf of its shareholders.

**Executive Summary**

The Re:Think discussion paper lists the objectives as achieving fairness, simplicity and jobs growth through a better tax system. CCW proposes that wine taxation requires little change.

Simple changes to the Wine Equalisation Tax Rebate, supported by industry would remove market distortions and ensure the scheme continues to support regional producers and the many winegrape growers whose business rely on these producers.

An increase in the level of taxation of wine products, whether through a change from *ad valorem* taxation to an excise system based on the amount of alcohol (like that applied to beer and spirits) or otherwise – risks devastating the wine industry while it is still restructuring and seeking to address low levels of profitability and excess supply of wine grapes.

It is true that CCW and, its business partner, Accolade Wines, are likely to suffer greatly if a uniform rate of volumetric taxation is introduced. Much of the fruit produced by CCW and the resulting wine sold by Accolade Wines is sold at lower price points, which are the price points most likely to be heavily impacted by a volumetric tax.

### Our Recommendations:

* No increase in taxation on wine;
* Tax structure to remain as “*ad valorem*” (value based);
* Oppose the introduction of a volumetric tax, essentially an excise system, which would introduce regulatory and administrative complexity and unnecessary compliance costs to already struggling wine businesses;
* Wine Equalisation Tax (WET) rebate to be restructured in line with the original intent, removed from bulk and unbranded wine as per the Winemakers Federation of Australia (WFA) recommendations – and a portion of savings reinvested in marketing Australian wine to the world.

### Introduction

CCW welcomes the opportunity to make a submission to the Federal Government’s Tax Discussion Paper, Re:think.

Our submission focuses on issues raised in Chapter 9 of the paper relating to indirect taxes that currently apply to alcohol. Our position supports the maintenance of the current value based tax for wine products.

### CCW Co-operative Limited

CCW Co-operative Limited (CCW) is the result of the merger of two Riverland co-operatives – Berri Co-operative Winery & Distillery Ltd and Renmano Wines Co-operative Ltd – both of which were established in the early 1920’s.

In 1989 CCW was restructured, forming the publicly unlisted company Berri Renmano Limited, now Accolade Wines Australia Limited, (formerly BRL Hardy Limited then Constellation Wines Australia) and shifted its equity holding into the International Wine Investment Fund (formerly the Wine Trust of Australia). CCW is now the preferred supplier of wine grapes to Accolade Wines Australia Limited.

CCW is a shareholder group of 577 wine grape growers in the Riverland area of South Australia. This represents approximately 50% of the wine grape production of the Riverland. In vintage 2015, CCW members supplied about 191,000 tonnes of grapes into the Accolade Wines Berri winery of the total 215,000 tonnes processed by the winery. CCW is the largest independent grape grower group in the country. Many of the wine grape shareholders are small to medium-sized primary producers.

### The Riverland Region

The Riverland is the largest wine growing region by volume in Australia and is responsible for about 25% of Australia's total crush and over 50% of South Australia's. The industry contributes significantly to the $1.2bn Riverland GDP and its direct impact is worth in excess of $275m. It influences the direct employment of over 3,000 people within the local community and indirectly, the industry has influenced the creation of over 12,000 jobs.

The Riverland, along with the Murray Valley region (near Mildura in Victoria) and the Riverina region of NSW are part of what is referred to in the industry as the “warm inland” regions. The warm climate dictates that the majority of fruit grown is used in various wine brands in the “Popular Premium” category of bottled product as well as cask wines. There are some boutique producers in the region producing limited amounts of wine that sells for approximately $30 per bottle but the vast majority of production is used in the own branded sub $10 bottle product and cask wines. The retail prices that can be commanded for bottled wine have decreased in absolute terms over the past seven years as the combined challenges of an unfavourable exchange rate, the global financial crisis and the imbalance between supply and demand have negatively impacted the industry. While a significant amount of wine produced in the region is exported, it is vital that a viable domestic market can underpin export growth**,** hence the importance of sound domestic taxation policy.

As a result of unfavourable domestic and export market conditions the region has suffered a reduction in farm gate income of wine grape sales from approximately $255 M in 2002 to an estimated farm gate income of $104 M in the recent 2014 vintage. The average price of wine grapes per tonne in 2002 was $674 compared to $288 estimated value per tonne in 2014, which is currently below the long term cost of production for all but the largest and most efficient producers. The reduction in regional income has flow-on effects to allied industries in the region including transport companies, irrigation utilities and agricultural supply companies but also companies that supply goods and services throughout the community.

The low returns have had a strong impact on growers, with many smaller growers choosing to leave the industry in 2008/9 with the assistance of the Small Block Irrigators Exit Grant. The area under vineyard in the Riverland has decreased by 7% since 2008 and the CCW Co-op shareholder base has declined from 741 members in February 2004 to 577 members as at December 2014. The Riverland region has experienced a decline population over the past eleven years. Since 2004 the population has declined about 5%, from 35,189 to 33,352[[1]](#footnote-1) in 2014.

In many ways, the Riverland and other warm inland wine growing regions of Australia have done the heavy lifting of the wine industry restructure; reducing planted area, reducing production capacity and increasing the efficiency of the larger vineyards that remain. This restructure has come at considerable cost to these wine growing communities.

### Anticipated Effect of a Volumetric Tax

If a volumetric tax were to be applied to wine at a similar rate to beer, the impact on the wine growing regions producing cask wines and bottled wine in the “Popular Premium” category would be devastating. None of the pain of restructuring that has been experienced in the past few years would compare to the overnight restructure that would occur once a volumetric tax was imposed.

If wine was taxed at the same rate as beer on a volumetric basis:

* It is estimated that 82% of wine would increase in price, leading to a fall in demand for grape products that are destined for cask wine and bottled wine retailed at $27 or below[[2]](#footnote-2);
* Wine sales of the average wine product from warm inland regions would fall by an estimated 41% using an “expected scenario”, with a corresponding decrease in the volume of grapes processed[[3]](#footnote-3);
* Significant job losses would occur, potentially including small producers forced out of business due to loss of WET rebate;
* The adverse impacts on grape growers and their communities will be concentrated on the inland irrigated regions in SA, Victoria and NSW; and
* There would be potentially unworkable implementation, substantial compliance costs and business disruption associated with an excise tax.

The projected losses in associated businesses and industry utilities such as irrigation trusts would also be serious. One element that distinguishes the wine industry is its regional footprint. The flow on effect to the Riverland and other warm inland wine producing regions will be considerable if the wine industry is put further in jeopardy with decreased wine sales due to additional taxation.

### The Wine Industry – Points of Difference

***Wine is a regionally based agricultural product that makes a significant contribution to the national economy, and warrants a different tax regime to that applied to beer and spirits.***

The majority of wine producing countries tax their industry less than other alcohol beverages (eg: beer and spirits). This is in part because of the significant contribution wine makes to both regional and national economies. Unlike beer and spirits, wine is a regionally based agricultural product that employs rural Australians, supports primary industries, establishes tourism destinations and creates direct and indirect regional employment[[4]](#footnote-4). According to the WFA, wine contributes the most of all the alcohol sectors to Australia’s economy[[5]](#footnote-5). Any change to the status quo in alcohol taxation has the potential to devastate regional communities and threaten jobs in those communities.

**Wine’s Contribution to the Economy and Regional Importance**

According to a recent report prepared by the WFA, the wine industry contributes:

* $1.77 billion to the national economy, most of which is reinvested into regional Australia (which is 14 times more than the spirits industry and 1.5 times more than beer);
* Provides 60,000 jobs, 16,122 which are direct jobs, mostly in regional Australia (which is 20 times more than spirits and 4 times more than beer). This contribution is made across 64 wine producing regional communities[[6]](#footnote-6); and
* $8.2 billion through wine tourism[[7]](#footnote-7).

A volumetric tax will significantly impact wine producers, and the regional employees and suppliers, dependent on them. These impacts will be particularly felt in Australia’s warm climate regions which includes the Riverland, as these regions provide a higher proportion of the wines in the price brackets that will be most impacted by any price intervention via the imposition of an excise based tax[[8]](#footnote-8).

In addition, any fall in demand for wine resulting from the imposition of a volumetric tax will lead to a decrease in demand for grape products (with little opportunity to export) with a loss of direct employment in the local wine industry and flow on effects to the regional economy.

Taking a broader perspective, a reduction in the volume of wine consumed within Australia would also have a significant negative impact on the competitiveness of Australia’s wine producers on an international level. This would occur due to a reduction in the economies of scale currently available to our wine producers including our partner Accolade Wines. The reduction in volumes of wine produced for the domestic market would increase the fixed costs carried by each unit of wine, including those produced for export markets, significantly reducing Australia’s competitiveness in an already difficult environment.

**Other Points of Difference**

It is also worth noting that wine is quite different to beer and spirits in a variety of other ways that make it vulnerable to any change in taxation. These differences have recently been highlighted by the WFA:

* Wine is the least profitable of the alcohol manufacturing sectors in Australia;
* Wine is the only net exporter, exporting AUD$2 billion per annum (12 times more than spirits and 39 times more than beer);
* Wine is the least consolidated sector;
* Retailer margins are greater on wine than beer and spirits (reducing the profit for grape growers and winemakers);
* Wine is more capital intensive than beer;
* Invested capital required to generate $1 of profit is higher in the wine industry;
* The wine industry needs a higher level of working capital than beer and other beverages; and
* Average return on invested capital for wine is less than 1% in contrast beer is 20.3%[[9]](#footnote-9).

Finally it is worth mentioning retail margins. Retailers generate more margin on wine sales than they do from beer and spirits. For example, Woolworths Liquor Group earns 2 to 3 times more margin on wine than beer. This reflects the highly fragmented Australian wine industry structure and the ease of the large retailers passing on costs to wine producers[[10]](#footnote-10). In light of the current retail power in the Australian wine industry, we anticipate that any increase in the cost of wine (that may occur if wine taxation were to increase) would be passed onto the wine producer (and not passed onto the consumer or borne by the retailer), further eating into the already small profit margin of the industry and reducing any possible positive social policy outcome that the anti-alcohol lobby may pursue.

## Flawed Arguments in Favour of Volumetric Tax

CCW believes that the ad-valorem Wine Equalization Tax (WET) that is currently used for taxing wine is working, albeit with aspects that need reform. There are a number of arguments that have been put forward in favour of changing the current ad-valorem wine taxation system to a volumetric tax. These arguments in favour of changing the taxation regime include the following:

* *A volumetric tax will be simpler to administer than the current WET;*
* *The taxation of alcohol should be uniform;*
* *The WET rebate is misused, and has now become excessively claimed beyond the intent and spirit originally intended;*
* *The current system encourages production of cheap wine which is contributing to the current oversupply problems the industry faces;*
* *Introduction of a volumetric tax will help to bring about the industry restructure needed*
* *There is a need to reduce sales of cask wine, as it is the cheapest standard drink and therefore is the cause of alcohol abuse.*

There is strong evidence that a volumetric tax will not be the “simple fix” as proclaimed by some, and that it will not address the need to address antisocial drinking habits. CCW agree that measures must be taken to curb alcohol abuse in society, but these measures must be targeted rather that the blunt administration of a tax. The common arguments in favour of changing the current wine taxation system to a volume based tax are addressed below.

***A volumetric tax will be simpler to administer than the current WET.***

Should a volumetric tax be imposed, the level of complexity and the cost will depend on the rate of taxation that is chosen. Far from being a good measure to address the perceived complexity of taxation between different alcoholic beverages, it is more likely that the administration, auditing and accounting of a volumetric tax will be more complex and time - consuming than is currently the case with the WET.

Because the level of alcohol cannot be rigidly controlled in wine as it can with spirit and beer manufacture, the final alcohol content of wine is not “created”. It must be determined through testing. Wine grapes are harvested when the flavour dictates that the desirable wine style will be achieved. One variety, or even a single patch of wine grapes may be harvested at different maturity levels in successive years, resulting in wines with different alcohol content. Each wine will therefore need to be tested to determine the taxation liability. This will create an additional level of monitoring and cost for wine companies, and is highly likely to need government excise auditors to assess the tax liability of each winery site. If the rate of taxation is not rigidly audited, there may be large variation in the amount of taxation liable.

***The taxation of alcohol should be uniform***

There is a common argument in favour of a volumetric tax that suggests that wine is taxed “incorrectly”, and that the current system is “wrong”. Some recent reports have referred to the current wine taxation as “illogical” and “perverse”. This is despite the fact that the vast majority of goods sold are taxed according on value.

*The fact that the taxation regime is* ***different*** *does not mean that it is “****wrong****”.*

There is different logic in imposing taxes – one reason is to change consumptive behaviour and another is to raise revenue. If the intent is to raise revenue, the method of taxation that imposes the least market distortion is an *ad valorem* tax. The more expensive a product is; the more tax is paid. If the intent is to change consumptive behaviour, such as suggested with a volumetric tax, then there must be clear evidence that the correct outcome will be achieved. The bulk of evidence suggests that this will not be the case with a volumetric tax on wine. In addition it will have the effect of creating the greatest market distortion by making the most expensive wine markedly cheaper, and by creating the greatest increase in floor price at the low price end of the market.

Much of the colourful language currently used to criticize the current tax system points out “preferential treatment” of lower price wine, and criticises the lack of price penalty based on price per standard drink. There is no less logic or credibility in criticising a volumetric tax for a bias toward regular consumers of expensive wine, who have the greatest capacity to pay tax.

Many arguments also criticise the disparity between the levels of taxation that is applied per standard drink across many types of beverages. The assumption that the taxation should be uniform is illogical – it infers that the only reason consumers choose a beverage is solely based on the percentage of alcohol it contains; and that consumers will make purchasing decisions based on the cost per standard drink rather than other parameters such as flavour, brand status, occasion, and matching the beverage with food.

It was the recognition that wine is unique as a sector, and that wine production is substantially different from spirits and beer that led to the formation of the WET in its ad-valorem form. The reasons for this sectoral difference still hold today.

***The WET rebate is misused, and has now become excessively claimed beyond the intent and spirit originally intended***

This may be the case, but if part of the taxation system is not working as originally intended, does it justify changing the entire system? CCW would suggest that if the WET rebate is not functioning as originally intended, and indeed if rebates are being excessively claimed, then the WET rebate should be reformed. CCW supports the Winemakers Federation of Australia recommendations on reforms to the WET rebate.

***The current system encourages production of cheap wine which is contributing to the current oversupply problems the industry faces***

***and***

***The introduction of a volumetric tax will help to bring about the industry restructure needed.***

This is not true. The current problems with the imbalance between supply and demand have been caused by planting of a total vineyard area in excess of the need to meet the perceived export markets, combined with a contraction in international demand for wine on the back of the recent global financial crisis and the recent currency pressure. It is stretching credulity to claim that the scale of expansion during the growth period was caused or indeed encouraged by a taxation system rather than commercial business decisions based on optimistic growth forecasts. The recent currency pressure may have caused the diversion of some wine that was destined for export back onto the domestic market, but the current production levels are not the direct result of domestic taxation policy.

It is in this light that CCW is concerned about the potential fallout of a volumetric tax. Much focus is given to the national situation in relation to the imbalance between supply and demand, but little focus is given to the *regional* supply and demand.

For many years the supply and demand statistics released by Wine Australia (formerly known as the Australian Wine and Brandy Corporation) have shown that that for reasons of cost of production (and the resulting price that can be sustainably paid for wine grapes) and flavour profile the fruit from warm inland regions should theoretically be balanced in regard to supply and demand. Riverland fruit has, however, been substituted with fruit from cool and coastal areas that has been sold by distressed sellers in these regions at unsustainable prices.

The Riverland region has recently lost 7% of the vineyard area, and the Murray Valley Wine Grape Growers Association area near Mildura in Victoria estimates that it has lost approximately 50% of its grape growers. These regions have already reduced the vineyard area by an amount close to the average 20% reduction that was suggested under the wine industry restructure agenda. If there is further stress in warm inland regions due to the imposition of a volumetric tax it is likely that vineyard removal will be overdone in areas such as the Riverland. This will be to the detriment of the entire Australian wine industry in terms of the impact on the desired price and flavour profile of wine grapes.

Considering that the profitability of wine brands is challenged at present, it is difficult to see how significantly increasing the retail price through taxation will help. The oversupply of wine has resulted in wine brands losing value in absolute terms over the past six years. This has led to downward pressure on retail prices of wine, and subsequently the fruit that is used to make them. The greatest challenge facing the industry is the ability to regain this value, and return to profitability along the supply chain.

A volumetric tax would create the greatest distortion in the market. Both low cost bottled wine and cask wine products would suffer the greatest increase in retail price above current levels. All this increase in retail price would be due to tax; none of this price increase would be returned to processors or growers. After such price increases it will be more difficult for brand owners to command better prices in future so that contributors to the products can return to sustainable profit margins.

Considering the magnitude of impact on the Riverland region in light of the recent restructure that has already taken place, it is more likely that introduction of a volumetric tax would be severely detrimental to the process of restructure of the wine industry rather than aiding it.

***There is a need to reduce sales of cask wine, as it is the cheapest standard drink and therefore is the cause of alcohol abuse***

Just because cask wines are the cheapest form of alcohol it does not necessarily follow that the majority of consumers of this wine abuse alcohol. Furthermore, despite the effects of a potential volumetric tax, *some* form of alcohol will still be the cheapest in terms of cost per standard drink, and therefore the “theoretical” first choice for drinkers with an alcohol problem. When the tax was increased on “Ready To Drink” (RTD) products, drinkers switched from RTD’s to full strength spirits. It is worth noting that these drinkers did not change their preferred drink of choice to cask wine or low priced bottled wine. Problem or habitual drinkers will switch to another form of alcohol rather than curb their drinking habits, so it is difficult to see the social benefit in this outcome.

The effect of a tax in curbing problem drinkers is highly debatable. Problem drinkers are the most insensitive to price. The consumers that are most likely to be deterred due to a price rise are the moderate drinkers.

While it is unquestionable that some consumers abuse cask wine, there is little evidence that cask wine is responsible for widespread levels of alcohol abuse across the community, and that the current method of taxation is not encouraging undue, excessive or “favourable” consumption of cask wine.

Not only do cask wines play a role in moderate drinking patterns, they are also an environmentally friendly form of packaging in terms of transport cost and ease of recycling, due to the weight and packaging material used.

The concern does not only rest with sales of cask wine. A volumetric tax at the beer rate would cause the price of 82% of wine sold in Australia to increase. In fact all wine that currently sells for a retail price lower than $27 per bottle would increase in price if the excise level of volumetric tax is set at this rate.[[11]](#footnote-11) This means that anyone who enjoys wine that sells for less than $27 per bottle will be negatively affected by a volumetric tax at this rate.

# Conclusion

CCW believes that the imposition of a volumetric tax on wine would be severely detrimental to the industry, the Riverland community and in particular the 577 individual grower businesses that we represent.

Our partner, Accolade Wines, have already indicated that any proposed introduction of this type of taxation will result in an initial reduction of their intake of fruit from the Riverland region by 30-40%. The result of a reduction to intake of this size, some 60,000 to 80,000 tonnes, directly affects the viability of our growers. Already, the pain is being felt from the downturn in farm gate income of 64% over the past 12 years. The membership base of our co-operative has also seen a reduction of one in five growers in the same period.

In addition to reduced incomes, over the course of the last 10 years growers have endured significant downturns in the value of “balance sheet” items. The consequences of this are many and mostly negative. Property and asset values have made it difficult for growers to invest and in many cases it has become impossible to borrow funds, not for further development, but to encourage best practice maintenance and diversification. Banks are also facing difficult decisions inasmuch as they know there can be no further extension of credit and it has become extremely difficult to take security over borrowings.

The “Re:think” discussion paper lists the objectives as achieving fairness, simplicity and jobs growth through a better tax system. CCW argues in this submission that changes to the existing wine taxation system will achieve none of these, and will more likely cause less fairness, increase complexity and cause a significant loss of jobs in the Riverland area.

CCW is in favour of retaining the current ad-valorem taxation of wine, with a revision of the WET rebate to ensure that misuse or rorting of the rebates can no longer occur and that the rebate regains its intended purpose.

1. ABS (2015), No. 3218*“Regional population growth”* [↑](#footnote-ref-1)
2. *Licensees’ liquor guide, 2010* [↑](#footnote-ref-2)
3. Deloitte Access Economics (2012), *“Regional economic impact of volumetric taxation of alcohol”* [↑](#footnote-ref-3)
4. Supporting Australian Wine (2011), *Submission to the Federal Government October 2011 Tax Forum,* (September, 2011), page 3. [↑](#footnote-ref-4)
5. WFA (2015), *Why should wine continue to receive a differential tax rate compared to other alcohol types?,* Adelaide: Winemakers’ Federation of Australia, page 1. [↑](#footnote-ref-5)
6. Supporting Australian Wine (2011), *Submission to the Federal Government October 2011 Tax Forum,* (September, 2011), page 3. [↑](#footnote-ref-6)
7. WFA (2015), *Why should wine continue to receive a differential tax rate compared to other alcohol types?* Adelaide: Winemakers’ Federation of Australia, pages 1 – 2 and Evans, Paul (2015), *Business Insider, “*Australians are Getting Hammered When it Comes to Wine Taxes”, 5 May 2015. <http://www.businessinsider.com.au/australians-are-getting-hammered-when-it-comes-to-wine-taxes-2015-5>. [↑](#footnote-ref-7)
8. WFA (2011), *Submission to Tax Forum*, (September, 2011), Adelaide: Winemakers’ Federation of Australia. [↑](#footnote-ref-8)
9. WFA (2015), *Why should wine continue to receive a differential tax rate compared to other alcohol types?* Adelaide: Winemakers’ Federation of Australia. [↑](#footnote-ref-9)
10. WFA (2015), *Why should wine continue to receive a differential tax rate compared to other alcohol types?* Adelaide: Winemakers’ Federation of Australia, page 5. [↑](#footnote-ref-10)
11. *Licensees’ liquor guide, 2010* [↑](#footnote-ref-11)