FARE submission on the Re:think tax discussion paper





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About the Foundation for Alcohol Research and Education

The Foundation for Alcohol Research and Education (FARE) is an independent, not-for-profit organisation working to stop the harm caused by alcohol.

Alcohol harm in Australia is significant. More than 5,500 lives are lost every year and more than 157,000 people are hospitalised making alcohol one of our nation's greatest preventative health challenges.

For over a decade, FARE has been working with communities, governments, health professionals and police across the country to stop alcohol harms by supporting world-leading research, raising public awareness and advocating for changes to alcohol policy.

In that time FARE has helped more than 750 communities and organisations, and backed over 1,400 projects around Australia.

FARE is guided by the World Health Organization's *Global Strategy to Reduce the Harmful Use of Alcohol*[a] for stopping alcohol harms through population-based strategies, problem directed policies, and direct interventions.

If you would like to contribute to FARE's important work, call us on (02) 6122 8600 or email info@fare.org.au.

a World Health Organization (2010). *Global strategy to reduce the harmful use of alcohol.* Geneva: World Health Organization.

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Overview

The Foundation for Alcohol Research and Education (FARE) welcomes the opportunity to provide a submission on the Australian Government's *Re:think tax discussion paper* (Discussion Paper). As an organisation working to stop harm caused by alcohol, FARE's submission focuses on alcohol taxation.

The current alcohol taxation system is illogical, incoherent and does not adequately recognise the extent of harms that result from the consumption of alcohol in Australia. The most illogical part of the alcohol taxation system is the Wine Equalisation Tax (WET). Under the WET, wine and other fruit-based alcohol products are taxed based on their wholesale price, rather than alcohol content. All other alcohol products like beer and spirits are taxed on a volumetric basis, albeit at different rates, with the amount of tax paid determined by the volume of alcohol within the product and the category of alcohol (for instance, full-strength packaged beer is taxed differently to spirits).

The WET has contributed to wine being the cheapest form of alcohol available for sale, with some wine in Australia being sold for as little as 24 cents per standard drink and the majority of bottled wine (65 per cent) being sold for under $8.00.[1] The Winemakers' Federation of Australia (WFA) acknowledges this, with Chief Executive Officer Paul Evans recently saying: "We believe that wine, at the retail point of sale, is too cheap."[2]

There is strong evidence to demonstrate that the lower the price of alcohol, the higher the levels of consumption.[3] In 2009, a meta-analysis was conducted of 112 peer reviewed studies on the effects of alcohol price and taxation levels on alcohol consumption and found that there was "overwhelming evidence of the effects of alcohol pricing on drinking".[4] Young people and heavy drinkers are particularly sensitive to alcohol price, with the heaviest drinkers more likely to seek out cheaper drinks than moderate drinkers.[5]

Pigovian or corrective taxes, such as alcohol taxation, have been used to change behaviours and prevent harms and to reduce the social costs of these harms on the community. Evidence clearly demonstrates that alcohol taxation reform is the most cost-effective measure to reduce alcohol harms. Alcohol taxation has also been found to be effective in reducing alcohol consumption and consequent harms among targeted groups (such as harmful drinkers and young people) and is cost beneficial.

There has never been a clearer case of reforming the alcohol taxation system. The support for reform is strong, with nine government reviews recommending overhauling the wine taxation system, including the Henry Review which determined that reforming the Wine Equalisation Tax (WET) was a matter of urgency for the Australian Government.[6] The public health sector, leading Australian economists and the majority of the alcohol industry are also supportive of reform.

A staged approach to alcohol taxation reform is needed in Australia and this should include immediate action to move the WET to a differentiated or category based volumetric tax rate, with the intention being to tax wine and other WET products at a rate that considers the alcohol content of the products. This staged approach should also include a longer term plan, based on clearly established public policy objectives that benefits the Australian community. The Australian Government can no longer delay reform and ignore the negative impacts the current alcohol tax system is having on the community.

This submission provides information in three sections, the first provides context on the current environment including the level of alcohol consumption and harms and the current alcohol taxation system. The second section focuses on the case for reforming the alcohol taxation system and the third outlines the policy responses needed. This submission makes nine recommendations to the Tax White Paper Task Force for reforming the alcohol taxation system, beginning with the WET.

Recommendations

The Foundation for Alcohol Research and Education (FARE) makes a total of nine recommendations to the Tax White Paper Task Force for reforming the alcohol taxation system.

1. That the Tax White Paper Task Force find that the current alcohol taxation system is illogical, incoherent and does not adequately recognise the extent and cost of alcohol-related harms in the Australian community.
2. That the Tax White Paper Task Force find that the most incoherent component of the alcohol taxation system is the Wine Equalisation Tax (WET), which must be reformed as a matter of urgency.
3. That the Tax White Paper Task Force find that alcohol taxation reform is the most cost effective way to reduce alcohol-related harms and that moving the Wine Equalisation Tax (WET) to a volumetric rate is cost beneficial.
4. That the Tax White Paper Task Force find that there is strong support for reforming the Wine Equalisation Tax (WET) from the public health sector, economists and the alcohol industry.
5. That the Tax White Paper Task Force adopt the following policy objectives for Australia's alcohol taxation system:
   i. Alcohol taxation must be applied according to the category and volume of alcohol within products and their potential to cause harm.
   ii. The economic externalities of alcohol consumption must be used to inform alcohol taxation rates.
   iii. Alcohol taxation must minimise distortion that may encourage harmful consumption of alcohol.
   iv. Alcohol taxation must ensure the cost of alcohol increases with average weekly earnings.
   v. Alcohol taxation must minimise loopholes.
   vi. Revenue collected from alcohol taxation should be used to pay for the costs incurred by Governments to address alcohol harms.
6. That the Tax White Paper Task Force recommend removing the ad valorem Wine Equalisation Tax (WET) and replacing it with a volumetric tax rate. This rate should be transitioned to a differentiated rate that is based on the alcohol content of wine.
7. That the Tax White Paper Task Force recommend that the Wine Equalisation Tax (WET) rebate be abolished.
8. That the Tax White Paper Task Force recommend than an industry adjustment package is only necessary to facilitate the need for structural change in the wine industry. This should be independent of the tax system.
9. That the Tax White Paper Task Force tax other products that fall under the Wine Equalisation Tax (WET) at appropriate levels based on their alcohol content, including:
   i. Moving cider to the current beer taxation arrangements, as cider has a similar alcohol content to beer. Where cider has added flavours it should continue to be taxed as a ready-to-drink beverage (RTD).
   ii. Moving 'Spirit' like products to the current spirit tax arrangement, as these products have a higher alcohol content and are marketed as spirits.

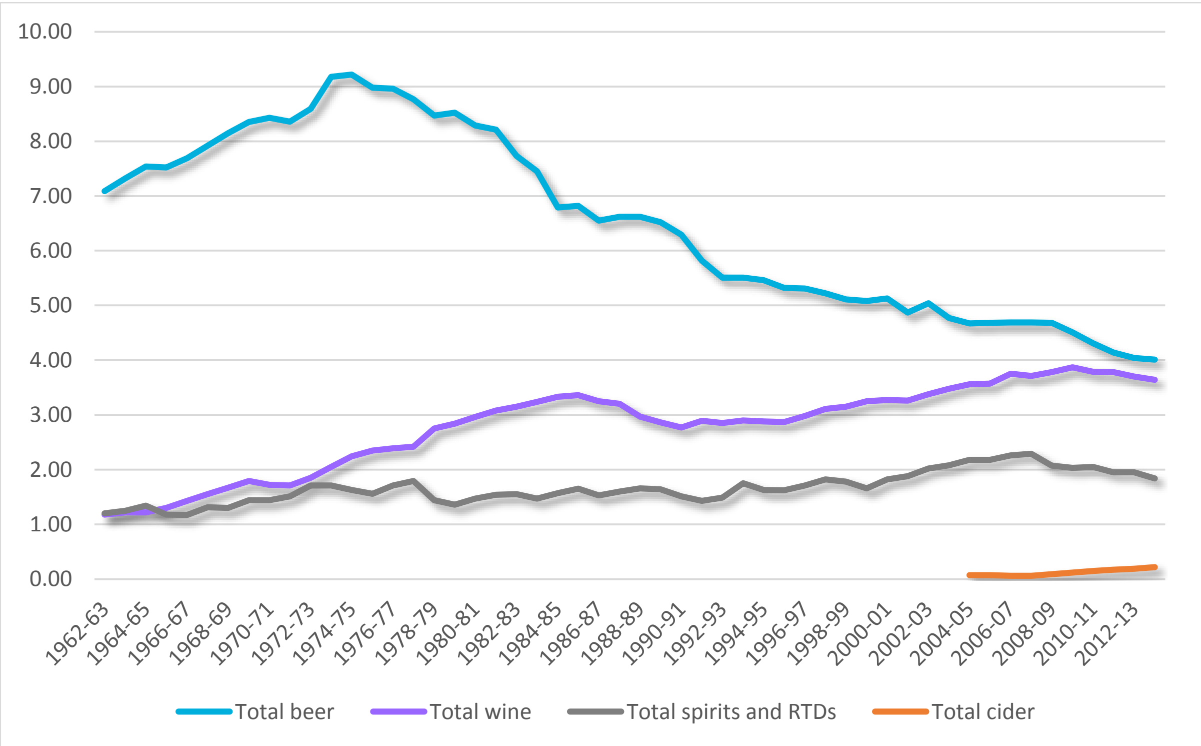
1. The environment

1.1 Alcohol consumption and harms

Trends in consumption by alcohol products

Apparent consumption of alcohol data produced by the Australian Bureau of Statistics (ABS) demonstrates that Australians aged 15 years and over consumed 9.7 litres of pure alcohol per capita in 2013-14. This equates to an average of 2.1 standard drinks per day.[7] This has remained relatively unchanged since the early 1990s. Over the last 50 years apparent consumption of alcohol has fluctuated, peaking at 13.1 litres of pure alcohol per capital in 1974-75.

When examining different products, the apparent consumption of wine has increased in Australia over the past 50 years, from 12 per cent of all alcohol (1.18 litres of pure alcohol per capita) in 1962-63 to 38 per cent (3.64 litres) in 2013-14. This is in contrast to beer which has almost halved from 75 per cent (7.09 litres of pure alcohol per capita) to 41 per cent (4.01 litres) over the same period. The apparent consumption of beer was at its highest during the 1970s and early 1980s, peaking in 1974-75 (9.22 litres of pure alcohol per capita) and has been declining since. Spirits (including ready-to-drink beverages) have increased from 13 per cent (or 1.2 litres of pure alcohol per capita) to 19 per cent (1.84 litres).[8] Unsurprisingly, the increased affordability of wine has coincided with this increase in the consumption of wine in Australia. The graph below highlights the trends in per capita consumption by products since 1962-63.



Source: ABS Apparent Consumption of Alcohol, Australia, 2013-14

Risky alcohol consumption in Australia

The National Health and Medical Research Council's (NHMRC) Guidelines *to Reduce the Health Risks from Drinking Alcohol* (Alcohol Guidelines) provide guidance for consumers about alcohol consumption. The two Alcohol Guidelines for healthy Australians aged 18 years and over are:

1. "For healthy men and women, drinking no more than two standard drinks on any day reduces the lifetime risk of harm from alcohol-related disease or injury".
2. "For healthy men and women, drinking no more than four standard drinks on a single occasion reduces the risk of alcohol-related injury arising from that occasion".[9]

When examining data from the *2013 National Drug Strategy Household Survey*, 6.5 per cent of Australians aged 14 years and older consume alcohol daily, with 18.2 per cent consuming alcohol in a way that puts them at risk of lifetime harm and 26.4 consuming alcohol at levels that place them at risk of short term harm.[10]

Further analysis of data from the *2010 National Drug Strategy Household Survey* demonstrates that 42 per cent of drinkers consume five or more standard drinks at least monthly, 15.8 per cent consume 11 or more standard drinks at least monthly and five per cent consume 20 or more standard drinks at least monthly. Understanding these consumption patterns is important because irrational, dependent consumption of alcohol is a market failure that alcohol taxation can address.

There are also differences in risky consumption by alcohol product. For example, cask wine drinkers are consuming alcohol more often and more on average than those who select other drink types as their main drink of choice, with 31.6 per cent of cask wine drinkers drinking daily.[11] More than one third (36.3 per cent) of cask wine drinkers exceed the guideline to reduce the risk of alcohol-related injury on a single occasion.[12] This is compared to 20 per cent of Australians in the same year (2010).

Alcohol-related harms in Australia

The harms from alcohol are significant. Each day 15 Australians die and 430 are hospitalised because of alcohol.[13] These figures largely do not acknowledge the significant impact of alcohol's harm to others, which include violence on our streets and in our homes, vandalism, road traffic accidents, child maltreatment and neglect.[14]

Across Australia, there are significant and increasing levels of alcohol-related harms. In New South Wales, for example, there was a 51 per cent increase in the number of alcohol attributable hospitalisations between 2001-02 and 2013-14[15] and in Queensland a 57 per cent increase in alcohol-related hospitalisations between 2002-03 and 2011-12.[16] In Victoria, an 85 per cent increase in family violence incidents involving alcohol between 2002-03 and 2012-13.[17] Nationally there has been a 46 per cent increase in the number of alcohol and other drug treatment episodes where alcohol was the primary drug of concern between 2002-03 and 2013-2014.[18]

1.2 The current alcohol taxation system

The current alcohol taxation system is illogical, incoherent and does not adequately recognise the extent and cost of alcohol-related harms in the Australian community. The alcohol taxation system is a complex arrangement with different levels of tax being applied depending on the type of product, their volume of alcohol, the way in which alcohol is packaged, the value of the product and in the case of wine, the size of the producer.

Beer and spirits are subject to excise duty which is a volumetric tax based on the alcohol content of the product. The rate is also adjusted twice a year in line with changes to the Consumer Price Index

(CPI). The excise for beer is imposed at eight different rates according to the volume of alcohol (light, mid-strength or full-strength), the type of packaging (draught or brewed) and whether brewed for commercial or non-commercial purposes. These rates currently range from $2.84 to $47.09 per litre of alcohol with the first 1.15 per cent of alcohol in beer tax-free.[19]

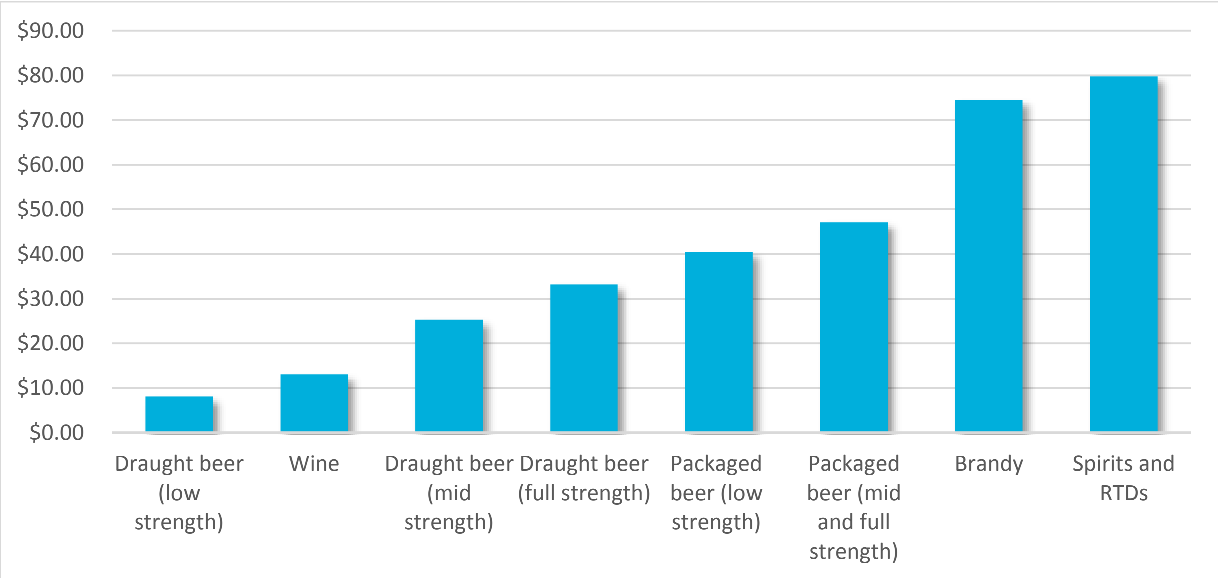
Spirits attract a higher rate of tax in light of their alcohol content, which can be up to 40 per cent alcohol content per volume, and their lower costs of production. The current tax rate for spirits is $79.77 per litre of alcohol.[20]

Brandy and *Other excisable beverages* (does not include beer, brandy or wine) are also subject to excise duty. The rate for brandy (a spirit distilled from grape wine) is $74.50 per litre of alcohol and the rate for *Other excisable beverages* (which exceed 10 per cent by volume of alcohol) is the same as for spirits, at $79.77 per litre of alcohol.[21]

The Wine Equalisation Tax (WET)

Unlike all other alcohol products, wine is taxed under a different regime to beer and spirits. It is subject to the Wine Equalisation Tax (WET) which is a tax based on the value of the wine. The WET was introduced on 1 July 2000 with the Goods and Services Tax (GST) as part of *A New Tax System* in order to maintain wine prices and revenue collection from wine sales, following the abolition of the 41 per cent wholesale sales tax that had previously operated. The WET therefore 'equalised' the price of wine to prices at prevailing levels.[22]

The WET applies not only to wine made from grapes but other fruit and vegetable based products with greater than 1.15 per cent alcohol by volume (ABV). These include cider and mead.[b] The tax is paid by wine producers, wholesalers and importers at 29 per cent of the last wholesale sale, which usually occurs between the wholesaler and the retailer.[23] The graph below highlights the different excise rates applied to products by category by pure litre of alcohol.



Source: Excise rates are current from the Australian Tax Office (ATO) as at 28 May 2015. The excise rate for wine was calculated from modelling by the Allen Consulting Group [c]

b Note that flavoured and coloured ciders are usually subject to excise rather than the WET, and attract the same excise rate that applies to ready-to-drink products (RTDs).

c Note that the excise rate for WET products of $13.03 is the amount calculated by the Allen Consulting Group for the report *Alcohol taxation reform – starting with the WET*. A rate of $13.03 would maintain revenue neutrality in 2011.

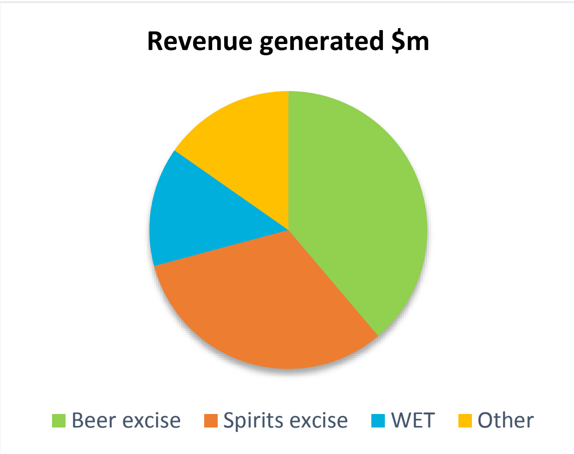
The application of the WET favours some products over others creating price signals that drive consumers towards lower cost, higher alcohol content products. The WET is applied regardless of the amount of alcohol in the product or harms associated with its consumption.

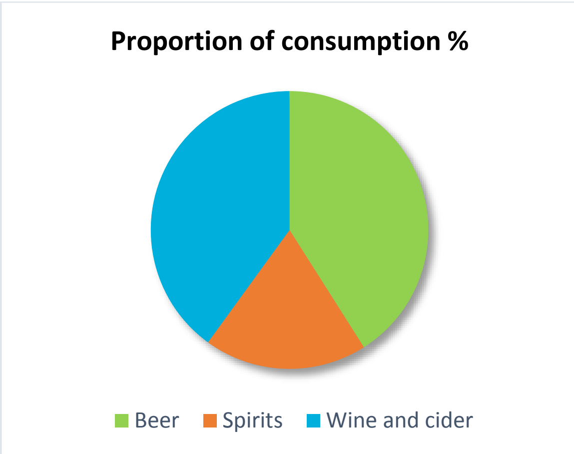
The WET creates a distortion, which results in larger volumes of cheap wine having favourable tax arrangements over quality wines. This also favours products taxed under the WET (including wine, cider and imitation spirits) over other alcohol products and products taxed under the WET (including wine, cider and imitation spirits) over other alcohol products. This approach does not meet the needs of the community in reducing harms, nor does it meet the needs of the wine industry in supporting smaller producers and local quality wines.

In addition, the production of cheap wine affects not only the wine produced for domestic markets but also those destined for export.[24] This is a risky strategy since this market segment is price sensitive, fiercely competitive on a global scale and operates on low profit margins.[25]

Because of its bias towards large producers, the WET has contributed to wine being the cheapest alcohol product available for sale in Australia with 65 per cent of sales for bottled wines being sold for under $8.[26] This is reflected in the average price per litre of Australian wine in 2012-13 which was $4.86.[27]

When comparing the revenue generated by beer, spirits, wine and cider and the proportion of consumption of these products, it is clear that the forgone revenue by government under the current tax arrangements is significant. The proportion of beer consumed in 2013-14 of all alcohol was 41 per cent, while the proportion of spirits was 19 per cent and wine and cider combined 40 per cent. The tax revenue generated from each of these products during the same year was $2,307 billion for beer, $1,902 billion for spirits, $908 million for other alcoholic beverages[d] and $826 million for wine. When looking at the proportion of total revenue by product, the revenue from beer was 46 per cent compared to 38 per cent for spirits, 18 per cent for other alcoholic beverages and 16 per cent for products under the WET.





Sources: Australian Budget Outlook 2013-14 and ABS Apparent Consumption of Alcohol 2013-14

The Wine Equalisation Tax (WET) rebate

In addition to the favourable tax arrangements for wine, a tax rebate was introduced in 2004 to support small rural and regional wineries in Australia. The WET rebate applies to all products subject to the WET. It is payable to eligible wine producers in Australia and New Zealand based on 29 per cent of the wholesale value of eligible domestic sales, up to a maximum of $500,000 each financial year.[28]

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[d] Other alcoholic beverages are those not exceeding ten per cent by volume of alcohol (excluding beer, brandy and wine).

Eligible producers are those that either manufacture the wine or provide the grapes to a winemaker to make the wine on their behalf.

In 2013-14 the Australian Government paid out a third of a billion dollars ($333 million) to Australian and New Zealand wine producers through the WET rebate. This is a form of corporate welfare that supports otherwise unprofitable business to continue operating.

In 2013 the Prime Minister, the Hon Tony Abbott, announced an end to corporate welfare, saying that his government was loth to give any more handouts to business. He went on to say that:

> *We don't want to see corporate welfare… we don't believe in corporate welfare… This government will be very loth to consider requests for subsidies, we will be very loth to do for businesses in trouble the sorts of things they should be doing for themselves… we are not here to sort of build a field of dreams.*[29]

While the WET rebate was originally introduced to support small producers in rural and remote areas in Australia, it is no longer achieving its objectives. Larger producers and producers from New Zealand are now eligible for the rebate and it does not appear to have helped smaller producers develop a greater presence in the market, since 90 per cent of production is sourced from 24 wine companies. Ongoing reports of 'rorting of the system' further undermines the intent of the rebate.

By supporting members of the wine industry that would not be economically viable without government assistance, the Government is directing skills and investments away from more productive activities which has implications for the economy.[30] If the Australian Government identifies that there is a need for an industry assistance package for the wine industry, this should be based on clear policy principles associated with an identified need. Assistance may be needed to support adjustment of the industry but any industry assistance package should be developed independent of the alcohol taxation system.

Recommendations

1. That the Tax White Paper Task Force find that the current alcohol taxation system is illogical, incoherent and does not adequately recognise the extent and cost of alcohol-related harms in the Australian community.

2. That the Tax White Paper Task Force find that the most incoherent component of the alcohol taxation system is the Wine Equalisation Tax (WET), which must be reformed as a matter of urgency.

2. The case for reforming the alcohol taxation system

2.1 Pigovian or corrective taxes are needed to address externalities

Taxes on alcohol and tobacco have been levied for centuries as a means of generating government revenue. The role of pigovian, or corrective, taxes is to address externalities caused by a particular product.

The application of pigovian taxes is an acknowledgement that a particular product, such as alcohol or tobacco, results in externalities. Applying such taxes is an efficient and effective way to correct these externalities. In recent decades, such taxes have been raised with the explicit objective of reducing the consumption of the targeted product on health grounds, particularly in regards to tobacco. Pigovian taxes should aim to modify health behaviours and maximise the benefits to the community.

The externalities of alcohol were described by Ken Henry as 'spillover costs'. Henry indicated that "while taxes on alcohol should not be used for general revenue-raising, they may have role in addressing the significant spillover costs on the community associated with alcohol abuse, by changing the price of alcohol faced by consumers".[31]

Since the Henry Review, numerous studies have attempted to determine what the externalities of alcohol are. Marsden Jacobs Associates (MJA) has described externalities as costs incurred by others beyond those considered and incurred by the individuals in a transaction. These costs are often not considered by the individual when they are purchasing or consuming alcohol.

MJA concluded that the total costs of alcohol harms in Australia would be easily in excess of $15 billion per year. In 2013-14, the government raised $5.1 billion in alcohol tax revenue. This is the tax on beer, spirits and other excisable beverages and $826 million in WET revenue (net of producer rebate).[32]

The tangible social costs of alcohol alone that result from an individual's alcohol misuse include an estimated $1.9 billion for healthcare, $2.2 billion for road traffic accidents, $1.6 billion for criminal justice and $3.6 billion in lost productivity, equating to $9.3 billion.[33] Third party costs or harm to others that arise from someone else's drinking have been estimated to amount to more than $14 billion in tangible costs. These costs include health care and child protection costs, lost wages and productivity, and out-of-pocket expenses such as property and personal damage, costs of professional counselling to cope with the drinker, and the cost of having to leave home and stay elsewhere to avoid the drinker.[34]

Other economists have made more conservative estimates of the social costs of alcohol. Often this work is commissioned by the alcohol industry and has significant shortfalls. In 2013, MJA assessed various public arguments relating to the externalities in response to the Australian National Preventive Health Agency (ANPHA) work regarding a minimum floor price for alcohol. In this work MJA, advised ANPHA that:

> *Great caution should be exercised in using the work of Crampton et al on which the industry submissions largely rely. The assumptions in this cost analysis do not accord with widely held Australian norms. For example, this work excludes costs that would derive to the society from a child born with foetal alcohol syndrome on the basis that this is a 'private cost'; other inappropriate assumptions have meant that this analysis yields costs ($3.8 billion) well below those derived from an analysis based on assumptions and value judgements reflecting community preferences including as expressed in legislation.*[35]

2.2 Alcohol taxation is the most effective measure to reduce alcohol harms

Alcohol taxation is the most cost-effective measure to reduce alcohol harms. An analysis of alcohol harm prevention policies found that alcohol taxation was the most effective policy, had the most breadth of research and has been implemented across a range of countries. [36] The analysis found that alcohol taxation is effective, as it has the ability to reduce consumption and related harms but also provides a source of revenue.[37] A key element of alcohol taxation polices is its ability to target heavy drinkers.[38]

In 2009 the University of Queensland modelled the cost-effectiveness of a variety of alcohol harm intervention approaches. Health outcomes in this model were evaluated in terms of 'disability-adjusted life years' DALYs (measure of overall disease burden, expressed as the number of years lost due to ill-health, disability or early death) to determine changes in the incidence, prevalence and mortality of alcohol-related diseases and injuries due to each intervention. The modelling showed that volumetric taxation of alcohol would:

- be both cost-saving and have a high probability of being cost-effective
- prevent 11,000 DALYs
- have weak sensitivity in terms of decay in the policy's effect over time.[39]

Of all of the intervention approaches, setting a reasonable minimum price for alcohol through imposition of volumetric taxes on alcohol is the most effective means of reducing alcohol harms.[40] International research also shows that this is the most effective means of targeting harmful drinkers.[41]

The study found that interventions that target young people (such as increasing the minimum drinking age), hazardous and harmful drinkers (such as brief interventions) or alcohol dependence (such as residential treatment) were less effective.[42]

Volumetric taxation has also been found to be effective in reducing alcohol consumption and consequent harms among targeted groups (for instance, harmful drinkers and young people). Policies that increase the price of alcohol lead to a reduction in the proportion of young people who are heavy drinkers, a reduction in underage drinking, and a reduction in per occasion 'binge drinking'.[43] Recent research in the USA looked at the impact of increasing alcohol taxes on risky consumption levels and found that raising the price of alcohol through taxes was effective in reducing binge drinking. Specifically, the research found that a one per cent increase in price due to taxation resulted in a 1.4 per cent reduction in binge drinking (defined as drinking at or above levels associated with intoxication) by adults.[44] This research builds on the evidence for the effectiveness of increasing the price of alcohol through taxes in reducing not just overall consumption but high-risk consumption.[45,46]

Modelling by the University of Sheffield also found that, irrespective of income, the greatest effects of a minimum unit price (set at £0.45GBP, or $0.89AUD) were noted for harmful drinkers. Moderate drinkers were least affected by the minimum unit price in terms of alcohol consumption and spending. Compared with other groups, harmful drinkers on low incomes purchase more alcohol priced below the minimum unit price threshold. Consequently, this group would be affected most by the minimum price policy. Large reductions in consumption in harmful drinkers on low incomes would coincide with substantial health gains in terms of morbidity and mortality related to reduce alcohol consumption. According to the study, individuals in the lowest socioeconomic group would accrue 81.8 per cent of reductions in premature deaths and 87.1 per cent of gains in terms of quality-adjusted life years.[47]

2.3 Alcohol taxation reform is cost beneficial

The total costs and benefits of alcohol to society comprise both those to the individual (that is, the private costs and benefits to the drinker as a result of their decision to drink) and those to the public (the costs and benefits to others due to that person's drinking).[48] The significant costs associated with harmful alcohol consumption are spread across the Australian community through the taxation and welfare systems and via the cross-subsidies in Australia's medical and other insurance systems.[49]

Consumer preferences on whether to drink alcohol and/or how much and how frequently, determine the extent to which they pay for the consumption of others or benefit from the current arrangements. This represents a real opportunity cost for non-drinkers and moderate drinkers who subsidise the cost of alcohol-related harms caused by the drinking of others. For many, these preferences are influenced by the cost of alcohol.

The Henry Review's recommendation to reform the WET recognised that a volumetric tax rate applied to wine would remove production and consumption biases from the alcohol taxation system, reduce compliance and administration costs, and better target the health and social costs of alcohol consumption.

A benefit cost analysis undertaken by MJA in 2012 found that the majority of Australians (85 per cent) would be better off from changes to the alcohol taxation system.[50] The benefit cost analysis extended the preliminary analysis by the Henry Review and examined the impacts of relevant reform scenarios on alcohol-related harms, consumer satisfaction and welfare, and government tax and revenues. It looked at the reduction in direct harm to others, the reduction in the harm to the drinker, the change in people's consumption decisions, changes in tax efficiency and changes in the efficiency of the resource allocation. It also examined different scenarios in relation to how to use the funds generated by increased tax revenue. These included a lump sum to each taxpayer each year, an equivalent increase in post-tax incomes by reducing Australian Government income tax, and an equivalent reduction in state and territory taxes through the Australian Government granting the jurisdictions the equivalent of the increase revenue from alcohol excise.

The benefit cost analysis found that reforming the WET would result in a clear benefit to moderate drinkers in light of the collateral damage they incur from others' harmful alcohol use.[51] These benefits derive from significant savings as a result of a reduced level of harm from others and increased disposable income through a rebate of increased alcohol excise back to taxpayers.

The analysis examined two scenarios where the WET and WET rebate were removed and replaced with a $29.05 excise (based on the excise for full-strength draught beer at the time). Results from the benefit cost analysis show that replacing the WET with a volumetric tax set at $29.05 per litre of pure alcohol is cost beneficial and would result in a net public benefit of $230 million per annum ($330 million per annum reduction in harms to others caused by alcohol and a net loss of consumer surplus of $100 million per annum) with benefits estimated to flow to 85 per cent of Australians.[52]
These figures are outlined further in the table over leaf.

	Change in welfare $ billion p.a.
Gross change in Consumer Surplus	–1.04
Rebate of increased taxation	0.94
Implementation costs	..
Net change in welfare	–0.10
Cost savings from reduced collateral harms	0.33
NET BENEFIT per annum	**0.23**

This benefit cost analysis demonstrates that a change to the WET, moving it to a volume based tax, would be cost beneficial to the community and particularly to moderate drinkers.

2.4 Nine government reviews have recommended reforming the WET

Nine government reviews have concluded that the alcohol taxation system should be overhauled. [e] In 2009, the Henry Review determined that reforming the WET was a matter of urgency for the Australian Government.[53]

The table over leaf provides an overview of some of the key inquiries and the recommendations made in relation to reforming the alcohol taxation system. It is important to note that the each of these reviews do not recommend the same taxation policy, but they all acknowledge that current alcohol taxation system needs reform, particularly the WET.

[e] Reviews that have recommended a volumetric tax be applied to wine include: the 1995 Committee of Inquiry into the Wine Grape and Wine Industry; 2003 House of Representatives Standing Committee on Family and Community Affairs Inquiry into Substance Abuse; the 2006 Victorian Inquiry Into Strategies to Reduce Harmful Alcohol Consumption; the 2009 Australia's future tax system (Henry Review); the 2009 National Preventative Health Taskforce report on Preventing Alcohol Related Harms; the 2010 Victorian Inquiry into Strategies to Reduce Assaults in Public Places; the 2011 WA Education and Health Standing Committee Inquiry Into Alcohol; the 2012 Australian National Preventive Health Agency Exploring the public interest case for a minimum (floor) price for alcohol, draft report and the 2012 Australian National Preventive Health Agency Exploring the public interest case for a minimum (floor) price for alcohol, final report.

Inquiry or review	Recommendation[f]
2003 House of Representatives Standing Committee on Family and Community Affairs Inquiry into Substance Abuse	The committee recommends that the Commonwealth Government investigate the social benefits of replacing ad hoc taxation on alcohol with an across the board regime based on alcohol content.
2009 Australia's future tax system (Henry Review)	All alcoholic beverages should be taxed on a volumetric basis, which, over time, should converge to a single rate, with a low alcohol threshold introduced for all products. The rate of alcohol tax should be based on evidence of the net marginal spillover cost of alcohol.
2010 Victorian Inquiry into Strategies to Reduce Assaults in Public Places	The Committee recommends that the Victorian Government, through COAG, supports and encourages the further investigation and modelling of a tiered volumetric system of taxation for alcoholic beverages to discourage harmful consumption and promote safer consumption.
2011 WA Education and Health Standing Committee Inquiry Into Alcohol	The Premier urgently negotiate with the Federal Government to increase taxes on alcohol products by introducing a tiered volumetric tax in addition to a minimum retail price per standard drink.
2012 Australian National Preventive Health Agency Exploring the public interest case for a minimum (floor) price for alcohol, final report.	Furthermore, based on public health considerations, the Agency finds that the current operation of the Wine Equalisation Tax is of concern and requires reappraisal.

Most recently alcohol taxation reform was explored by ANPHA (now located in the Department of Health). In 2011-12 ANPHA concluded that the WET required reappraisal.[54] In its final report, ANPHA stated that: “There was strong endorsement from a wide range of stakeholders for a volumetric tax on all alcohol products and many noted, referring to the Henry Tax Review, that reform of the WET could have similar effects in reducing alcohol-related harms as those of a minimum price.” [55]

The Henry Review stated that the “current alcohol taxes reflect contradictory policies… As a consequence, consumers tend to be worse off to the extent that these types of decisions to purchase and consume, which may have no spillover cost implications, are partly determined by tax”.[56] The Henry Review recommended that alcohol taxes should be set to address the spillover costs imposed on the community of alcohol abuse.

2.5 There is strong support of alcohol tax reform

There is substantial support for reforming the WET and WET rebate from a range of sectors across Australia. Support for reforming the WET is shared by public health advocates and researchers, several government reviews (as outlined above), leading Australian economists and a majority of the alcohol industry.

Within the alcohol industry, the Distilled Spirits Industry Council of Australia[57], Brewers Association[58], two of the largest wine producers in Australia and several smaller wine producers, are all supportive

f The recommendations are direct quotes from the final report of the Inquiry or Review.

of reforming the WET. There is a common misconception that the wine industry is not supportive of alcohol taxation reform. However the wine industry is very diverse with large, medium and small producers and large segments of the industry are now supportive of reform.

Treasury Wine Estates has stated that: "The phenomenon of very cheap wines seen in Australia in recent years is a further unintended consequence of the WET rebate, and adds weight to calls to remove or fundamentally reform the scheme".[59] Former Chief Executive David Dearie used stronger language in another forum, calling for the scrapping of the WET and WET rebate and saying that it is "widely rorted, underpins the excess supply that has blighted Australian wine".[60]

Pernod Ricard Winemakers (previously Premium Wine Brands) said that:

> *PWB believes that existing wine tax arrangements are distorting market forces by sustaining the 20 per cent of vineyards which the industry Wine Restructuring Action Agenda found to be surplus to market requirements and incentivising the production and sale of cheaper wines, contrary to the industry endorsed strategy of value building through premium, branded products. We believe that tax reform would end these distortions and allow normal market forces to address the structural oversupply issues….. PWB supports the reform of the wine tax system in Australia so that wine is taxed by alcohol content (i.e. a volumetric tax).*[61]

Treasury Wine Estates and Pernod Ricard Winemakers are two of the largest wine producers in Australia, making up 20.5 per cent of Australian wine production.

Commentary from within the wine industry suggests that there are several other small and medium sized producers who acknowledge that the industry would benefit from reforming the WET. Jeremy Oliver, an Australian wine writer and presenter has written: "Is there any sense in any aspect of the current taxation environment? If so, I can't see it. Surely it's time to fix this thing before the collateral damage it directly causes gets even worse."[62] Westend Estate Wines (now Calabria Family Wines) says that: "The Wine Equalisation Tax is having a negative impact throughout the domestic market, and virtual wineries with no long-term vision are abusing the system which was put in place to benefit the smaller wineries."[63]

Recommendations

3. That the Tax White Paper Task Force find that alcohol taxation reform is the most cost effective way to reduce alcohol-related harms and that moving the Wine Equalisation Tax (WET) to a volumetric rate is cost beneficial.

4. That the Tax White Paper Task Force find that there is strong support for reforming the Wine Equalisation Tax (WET) from the public health sector, economists and the alcohol industry.

3. Policy response

A differentiated volumetric alcohol taxation system is needed in Australia. A staged approach is required for reforming the current alcohol taxation system that prioritises changes to the WET, the most inequitable part of the taxation system. A longer term plan is also needed for alcohol taxation reform that addresses further inequities in the alcohol taxation system.

3.1 Policy objectives for Australia's alcohol tax system

Alcohol taxation reform must be based on clear policy objectives that aim to maximise benefits to the community in reductions in alcohol harms and externalities. FARE has developed six public policy principles for a more equitable alcohol taxation system and these are outlined below.

1. **Alcohol taxation must be applied according to the category and volume of alcohol within products and their potential to cause harm.**

Taxation is an effective levers for moderating alcohol consumption. Volumetric taxation is one of the most cost-effective means of preventing and reducing harmful alcohol consumption.[64] A differentiated volumetric tax on alcohol ensures that all alcoholic products are consistently taxed according to their alcohol content, within their product categories. Differentiated volumetric taxation can influence price in a way that simultaneously encourages the consumption of lower alcoholic products while discouraging the consumption of higher alcoholic products.

Evidence shows that low alcohol prices result in higher consumption levels, including heavier drinking, occasional drinking, and underage drinking. If the price of alcohol increases, a reduction in overall consumption, and heavy consumption in particular, is observed.[65] In 2009, a meta-analysis was conducted of 112 peer reviewed studies on the effects of alcohol price and taxation levels on alcohol harms. This study found that there was "overwhelming evidence of the effects of alcohol pricing on drinking".[66]

2. **The economic externalities of alcohol consumption must be used to inform alcohol taxation rates.**

Alcohol use results in a range of harms to individuals and the people around them. It is essential when assessing the externalities of alcohol that consideration is given to broad impacts of alcohol on individuals and others. It is important that a range of externalities that result from alcohol harms are considered when determining the rates of alcohol taxation. These externalities include the intangible third party costs of alcohol consumption such as lost productivity, family income foregone, and time caring for the family member with alcohol use problems. All tangible and intangible (such as loss of life, pain and suffering) third party costs of alcohol consumption must be included within a social cost as they are the costs borne by society. This issues needs to be addressed by policy makers as part of efforts to raise the welfare of society and address the market failures that contribute to irrational, dependent alcohol consumption.

3. **Alcohol taxation must minimise distortion that may encourage harmful consumption of alcohol.**

The inconsistencies in taxes applied to different alcoholic products create economic distortions whereby some products and producers are favoured over others. These inconsistencies and the resulting distortions violate the principles of efficiency and simplicity which the Henry Review has outlined as principles of an effective tax system.[67] In so far as they influence price, these inconsistencies also send confusing signals to consumers that certain alcoholic products should be preferentially consumed over others. Instead, tax and price should be used as a mechanism to signal to the consumer the volume of alcohol in the product and by implication, its potential for harm.

4. Alcohol taxation must ensure the cost of alcohol increases with the average weekly earnings.

Given that alcohol is continuing to become more affordable, it is essential that an alcohol taxation maintains the cost of alcohol products relative to Australian incomes and adjusted in accordance with the average weekly earnings. This currently occurs with tobacco products where excise is adjusted bi-annually based on average weekly ordinary time earnings. Maintaining the cost of alcohol products to these facts ensures that the cost of cheaper products continue to rise with other products on the market. The impacts of alcohol taxation reform on alcohol consumption and production must be regularly evaluated and alcohol taxation excise rates reviewed in accordance with this information. An agenda for alcohol taxation must include such ongoing evaluation and adjustment.

Reducing the alcohol-related harms experienced by Australians requires a range of responses, including pricing which has been demonstrated to be the most cost-effective policy response. Alcohol-related-harms in association with alcohol products getting cheaper are reason for immediate government action to address the availability of cheap alcohol products.

5. Alcohol taxation must minimise loopholes.

It is known that heavy drinkers tend to seek out the cheapest forms of alcohol however the effectiveness of increasing the price can be diminished if consumers are able to choose cheaper, lower quality products to compensate.[68] The alcohol industry has been quick to innovate and take advantage of the perverse incentives offered by the current taxation arrangements. An example of this is the 'spirit-like' products with an alcohol content of 22 per cent that are actually a wine based product therefore taxed under the WET are currently being produced and marketed like a spirit. It is essential that alcohol taxation do not provide the alcohol industry the opportunity to undermine policies that aim to reduce alcohol consumption and alcohol-related harms.

6. Revenue collected from alcohol taxation should be used to pay for the costs incurred by Government to address alcohol harms.

In Australia there is a significant gap between the tangible alcohol relevant costs and the amount of tax collected by the Government. In 2013-14, the Government raised $5.1 billion in alcohol tax revenue, this is the tax on beer, spirits and other excisable beverages. This is despite the economic impact of alcohol on the Australian community costing $14.3 billion. This is the tangible costs from the third party harms from alcohol, which consists of out-of-pocket costs, forgone wages or productivity, and hospital and child protection costs.[69] These costs are a significant underestimate of the total cost of alcohol-related harms as they do not consider those incurred by individuals or intangible costs that also result from alcohol. Revenue collected from alcohol tax should be used to reduce the disparity that exists between the amount of tax revenue received and the tangible costs of alcohol-related harms.

3.2 The need for a differentiated alcohol taxation system

A differentiated alcohol taxation system is needed that considers the alcohol content of the products within different product categories. There are three main reasons why a differentiated volumetric tax rate is needed, rather than a 'straight' volumetric tax rate. These are outlined below.

1. Public health reasons

Changes to alcohol taxation have been demonstrated to influence consumption and harms among specific high-risk populations including young people and heavy drinkers.[70] Alcohol taxation can also be used as an effective means for 'directing' consumers to beverages with lower alcohol content, which have a corresponding relationship with lower levels of alcohol-related harm (such as low or mid-strength beer).The public heath rationale for adopting a differentiated approach to alcohol taxation, rather than a straight volumetric tax is to ensure that changes in taxation do not result in the affordability of alcohol products increasing, which would result in increased consumption and harms.

An example of tax rates being applied for public health reasons was first seen with the introduction of different tax rates to beer. In 1984, the tax rate to low strength beer was lowered with the aim to encourage consumers to change products to a less harmful product and to reduce the incidents in road traffic accidents.[71] In 1988, changes were again made to tax rates on beer so that they were taxed in same way as spirits, on the basis of volume of alcohol. This change resulted in beer being taxed significantly less than spirits for the first time.[72]

Public health considerations were given to both these changes on the basis that the use of excise tax to effect a change in consumption towards a perceived less harmful product. As a result of the changes to tax rates of beer, low alcohol beer increased its sales significantly and captured approximately 20 per cent of the total Australian beer market.[73]

Case study: The Australian experience of the 'alcopops' tax

In July 2000, the Australian Government introduced the broad-based GST of ten per cent on goods and services sold or consumed in Australia. The introduction of the GST led to ready-to-drink (RTD) beverages being taxed at the same rate as full-strength beer. RTDs were consequently taxed at 40 per cent less per litre of alcohol when compared with straight spirits.[74]

The introduction of the GST led to reduced alcohol prices, increased sales and increased consumption of RTDs. As RTD producers exploited this tax advantage, prices were driven further down between 2000 and 2007. This made RTDs a substantially cheaper drink choice relative to other spirits. Premixed spirits was the major growth category in the Australian liquor market in the decade after 2000. RTDs' share of the total alcohol market increased from three per cent in 1999-2000 to 10.4 per cent in 2006-2007.[75] During this period, RTDs arguably not only competed for market share, but also increased the overall alcohol market in Australia.[76]

In April 2008 the Australian Government introduced the 'alcopops' tax on RTD beverages. The aim of the tax was to reduce harm from binge drinking among young people, as a group which are the primary target market (young females in particular) for RTD beverages. This brought the excise on spirit-based RTDs in line with the excise imposed on straight spirits at the time ($66.67 per litre of pure alcohol). In 2009 wine and beer-based RTDs were also taxed at the same rate as straight spirits and spirit-based RTDs. As a result, this policy increased the tax imposed on RTDs by 70 per cent. At the time, the Australian Government claimed that this measure closed "a loophole created in 2000 with the introduction of the GST which made RTDs cheaper than if consumers bought the spirits and mixed them themselves".[77]

In the two years following the introduction of the alcopops tax, sales data showed a decline in consumption of RTDs.[78,79] Assessments of sales data following the introduction of the 'alcopop tax' show that RTD sales reduced by approximately 30 per cent and 1.5 per cent in pure alcohol sales.[80] It is worth noting that these levels of reduction are not explained by the global financial crisis. Increased prices reduced consumption of RTDs and alcohol overall.

A recent study into the impact of the GST and 'alcopops' tax on the incidence of alcohol harms found:

- The GST (whose introduction led to reduce prices for RTDs) was associated with a statistically significant increase in Emergency Department (ED) presentations for acute alcohol problems among 18-24 year old females.
- The 'alcopops' tax (whose introduction increased the price of RTDs) was associated with a statistically significant decrease in ED presentations among 15-50 year old males, and 15-65 year old females, particularly 18-24 year old females.
- The alcopops tax was also associated with declining ED presentations in underage drinkers.[81]

2. Structural and cultural reasons

The different rates that are currently applied to beer and spirits have been applied not only for public health reasons but also for structural and cultural reasons. For example the tax rate applied to full-strength beer draught beer is lower than tax applied to full-strength packaged beer due to the differences in costs throughout the production, packaging and sale processes. Draught beer for example would carry more overhead costs due to the selling of beer at on-licence premises compared to selling packaged beer at off-licence premises. These structural factors play a role in determining the tax rate alongside the consideration of alcohol content.

Some products are taxed in different ways because there is an acknowledgement that they may be consumed in a way that produces harms. If a straight volumetric tax rate is applied to all products, this will result in spirits becoming relatively cheaper, because spirits are currently taxed at a higher rate than all other products. Spirits are traditionally taxed at a higher rate because spirits are cheaper to produce than other alcohol products and have the potential to cause greater harms due to the 'speed to intoxication' ratio. Put simply, it is easier to get drunk more quickly on spirits because of their high alcohol content and the way that they are traditionally consumed.

3. Historical reasons

It is also important to take into account the current alcohol taxation arrangements when examining options for changes to alcohol taxation. Currently, not all alcohol products are treated equally under the alcohol taxation system. Different levels of tax are applied depending on the type of product, their volume of alcohol, the way in which alcohol is packaged. Beer and spirits are subject to excise duty which is a volumetric tax based on the alcohol content of the product.

The excise for beer is imposed at eight different rates according to the volume of alcohol (light, mid-strength or full-strength), the type of packaging (draught or brewed) and whether brewed for commercial or non-commercial purposes. These rates currently range from $2.84 to $47.09 per litre of alcohol with the first 1.15 per cent of alcohol in beer tax-free.[82]

The different rates of alcohol taxation that currently exist need to be considered by decision makers in determining future arrangements, with particular attention given to the need to ensure that alcohol products do not become more affordable as this will lead to their increased consumption and harms. This is particularly important when considering changing the taxation rate applied to spirits, due to the difference in the current rates applied.

3.3 A staged approach to comprehensive alcohol tax reform

A staged approach for alcohol taxation reform must be established by the Australian Government. This approach needs to prioritise reforming the WET, the most inequitable part of the taxation system. Three phases to reforming the alcohol taxation system are proposed below.

1. Immediately replace the WET with a volumetric rate of taxation

As highlighted previously the WET is the most incoherent of the alcohol tax system and needs to be reformed as a priority. Problems with the WET include:

- In contrast to other products, products under the WET are an ad valorem tax that is based on the value of the product.
- The WET encourages the production of large quantities of cheap wine and in doing so, encourages consumption of excessive levels of low quality, cheap wine.
- The WET distorts production and consumption decisions and results in non-drinkers and moderate drinkers paying a disproportionate amount of taxation.

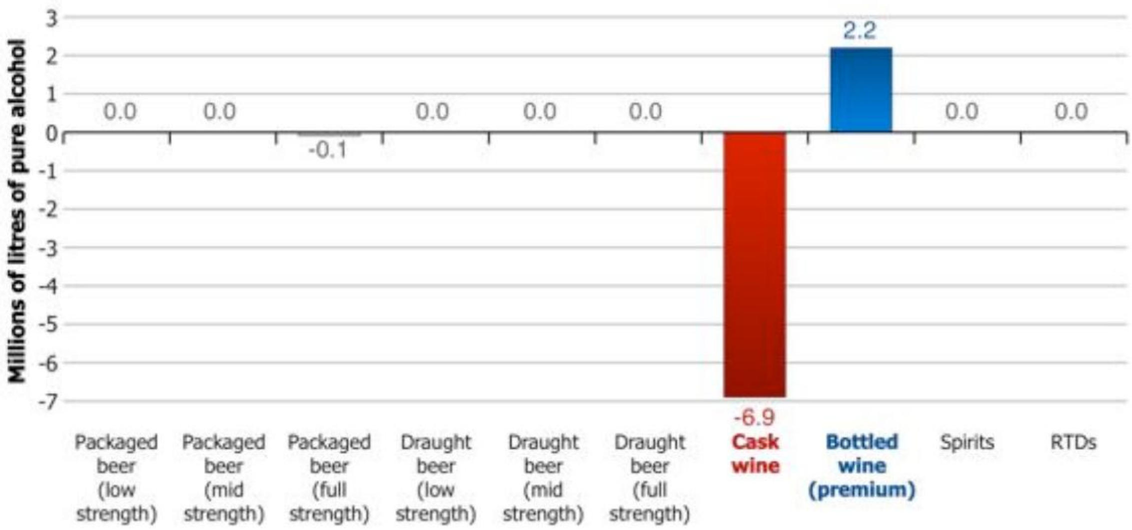
The WET must move to a volumetric tax rate as a matter of urgency. As a transitionary arrangement, the rate for wine could first be set at a rate that is revenue neutral with the WET revenue collected remaining at the same rate. Wine should then be transitioned to a rate that appropriately reflects its alcohol content.

To understand the impact of this transitionary arrangement, modelling undertaken by the Allen Consulting Group in 2011 can be used as an example of the impact of removing the WET and replacing it with a volumetric tax rate.

If the WET is removed and replaced with a volumetric tax rate for wine products which results in no changes to tax revenue (revenue neutral). The volumetric tax rate for this to occur is calculated at $13.03 per litre of alcohol. Applying this rate of tax to wine would result in:

- an increase in the price of cask wine of 24.7 per cent and a decrease in the price of premium wine by 3.9 per cent
- a decrease in consumption of cask wine by 26.2 per cent or 6.98 million litres of pure alcohol
- a 5.1 per cent increase in premium wine consumption, equitant to 2.2 million litres of pure alcohol
- substitution towards premium wine from other alcohol types by 1.8 per cent or 0.23 million litres of alcohol
- a decrease in total alcohol consumption of 2.6 per cent or 4.9 million litres of pure alcohol
- no change in revenue.[83]

The changes in consumption compared to the alcohol taxation arrangements as at 2011 are highlighted in the below graph.

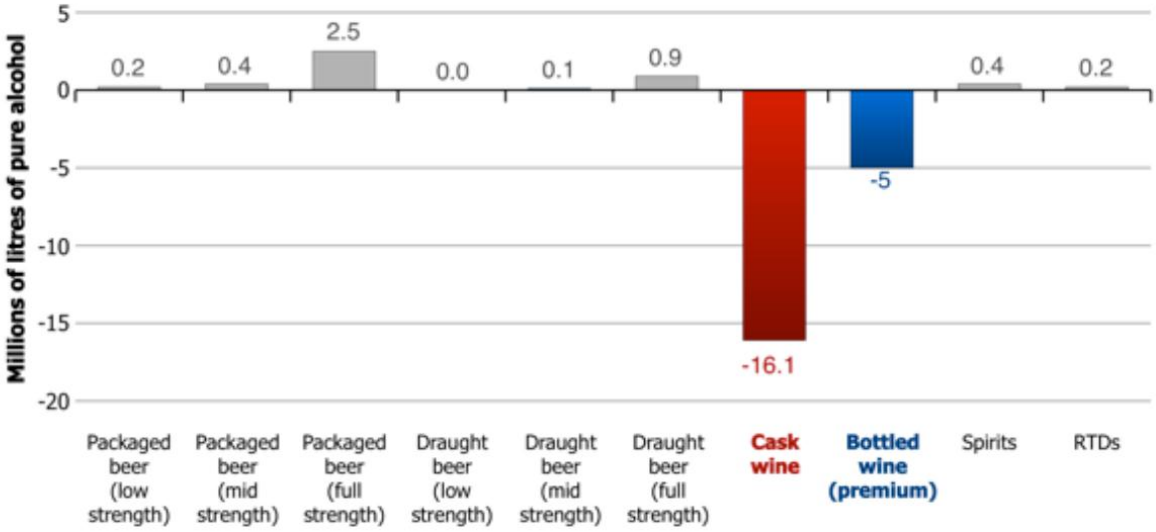


Source: Allen Consulting Group analysis, 2011

Once wine has been moved to a volumetric rate, consideration must be then given to a rate that is appropriately reflect alcohol content. An example of this is removing the WET and replacing it with a volumetric rate of packaged beer of $43.85 (the rate of packaged full-strength beer at the time the modelling was undertaken in 2011). Applying this rate to wine would result in:

- an increase in the retail price of cask wine of 114.6 per cent and an increase in the price of premium wine of 17 per cent
- a decrease in cask wine consumption of 61.2 per cent or 16.1 million litres of pure alcohol
- a decrease in premium wine consumption of 11.2 per cent or 5 million litres of pure alcohol
- an increase in alcohol as a consequence of people switching from wine to other forms of alcohol of 38.0 per cent or 4.7 million litres of pure alcohol
- a reduction in overall alcohol consumption of 8.6 per cent or 16.3 million litres of pure alcohol
- an increase in tax revenue of approximately $1.5 billion.[84]

The changes in consumption compared to the alcohol taxation arrangements as at 2011 are highlighted in the below graph.



Source: Allen Consulting Group analysis, 2011

2. Abolish the WET rebate and determine the need for an industry support package with a clear policy intent

The WET rebate provides a tax rebate of up to $500,000 to all wine producers in Australia, regardless of their size. In 2005 the rebate was extended to New Zealand wine producers and since this time New Zealand wine imports into Australia are estimated to have grown by 139 per cent.[85]

The WET rebate represents corporate welfare at its worse. It is no longer achieving its policy objectives and needs to be removed. It was originally designed to support small business in rural and regional areas in Australia however the intent of the policy has been undermined by its availability to all producers, by large producers taking advantage of tax loopholes and by the extension of the rebate to New Zealand producers. It also supports producers who would otherwise not be able to compete in the market and discourages consolidation because of the way in which the rebate is structured.[86] Together with the WET, the rebate perpetuates the circumstances that are damaging the reputation of the wine industry as a whole and grape growers in particular.

Members of the alcohol industry agree that the WET rebate needs reform. The WFA has stated that the WET rebate is being paid to foreign entities is '…completely at odds with the original intent of the rebate which was introduced to support small and medium sized Australian producers and the regional communities they operate in.'[87] In its 2014 Pre-budget Submission the WFA said that "there is a need to urgently reform eligibility to the WET rebate to ensure it is not accessed by unintended recipients. In particular, the extension of rebate entitlements to New Zealand and other foreign producers at a time when imports are directly damaging branded Australian wine businesses that support local communities should cease immediately."[88] It believes that the WET rebate should also be removed from bulk, unbranded and retailer "own brand" wine as the long-term future of the industry lies in strong branded product that can command loyalty and profitable margins from consumers and the highly consolidated domestic wine retail sector."[89]

Treasury Wine Estates says that "The Wine Equalisation tax (WET) rebate is a damaging subsidy that has negatively impacted the profitability and productivity of the industry. It is preventing consolidation and sustaining uneconomic production, at a time when the industry urgently needs to retire excess supply and rebuild value in the Australian wine category "The WET rebate should be abolished or, at a minimum, fundamentally reoriented to become a cellar door style rebate available only to the retail sales of genuine wine producers;"[90] Premium Wine Brands agrees saying that "Despite the fact that PWB currently benefits from the WET rebate we believe that its abolition would be in the best interests of the wine industry."[91]

Transitional assistance may be needed to support the industry through this change. In particular, smaller producers who are potentially successful but need temporary assistance, regional areas in which these growers and producers are located, and those who entered industry on the basis that assistance was available and that it would be ongoing, may need some form of assistance as the industry adjusts to the new arrangements. The Productivity Commission has identified reasons why a structural adjustment package might be warranted. The Allen Consulting Group has summarised these as follows:

Problem	The structural change needed is substantial.
Timeframe	The barriers to adjustment are long-term.
Safety Nets	The existing safety nets such as welfare payments, alternative employment or retraining opportunities are insufficient.
Unfair Disadvantage	The change burdens a group already disadvantaged in the community.
Unfair Advantage	The change assists a group already at an unfair advantage in the community.
Unexpected Change	The change will be unanticipated by market participants.
Facilitation	There will be significant opposition to the necessary changes to warrant pacifying opponents through assistance measures.
Transition	The assistance reducing the transition costs attributable to market impediments.

If an industry assistance package is required to support the alcohol industry, the policy objectives that underpins the support package should be clearly defined, based on identified policy principles associated with identified need and developed independently of the alcohol taxation system. The Productivity Commission has developed a set of general principles to guide selection of specific structural adjustment measures. Measures should:

- be targeted to those groups where adjustment pressures are most acutely felt and operate proactively as well as retrospectively
- facilitate, rather than hinder, the necessary change
- be transparent, simple to administer and of limited duration
- be compatible with general 'safety net' arrangements.[92]

The WET rebate should be removed as a matter of urgency and the Australian Government should determine whether an industry restructure package is needed and the policy objectives of such a package.

3. Move other products to a differentiated tax rate

The WET is not only applied to wine. It is also applied to other fruit and vegetable based alcohol products. These include cider, perry and mead. This also allows for a range of alcohol products to be produced from the fermentation of fruit or vegetables and for the WET to be applied to these products, regardless of their appearance, marketing or more importantly, their alcohol content.

The alcohol industry has been quick to innovate and take advantage of the perverse incentives offered by the current taxation arrangements. 'Spirit-like' products such as TriVoski or Divas Vodkat are examples of products that are produced to imitate spirits, particularly Vodka, but are actually 'wine based.' [93] Because these products are taxed under the WET and not at the higher spirits rate, they are able to be taxed as wine and sold at cheap prices. For example, a 750ml bottle of TriVoski containing 13 standard drinks can be purchased for $9.95. This equates to 77 cents per standard drink. Two 700mls bottles of Divas Vodkat can be purchased for $19.98, equating to 59 cents per standard drink.[94] These products are clearly marketed as spirits. Advertising on the Old Richmond Cellar website states that *"*DIVAS is not a cheap Vodka. It has none of the crass stereotypical qualities of cheap Vodka, such as nasty chemical burn, etc… DIVAS is 100% Australian made from real Australian wine grapes, allowing it to be priced as fortified wine, yet TASTES AND SMELLS EXACTLY LIKE TOP QUALITY VODKA!"[95] The Australian Government must question whether the intention of the WET was to allow the introduction and production of these alcohol products. TriVoski and Divas Vodak are depicted below.

Cider is also taxed under the WET. A recent report showed that per capita consumption of cider in Australia has increased by 150 per cent between 2007 and 2011. [96] Much of this growth and diversification into the cider market has coincided with the increased taxation applied to RTDs as a result of the alcopops tax introduced in 2008. Cider is subject to less taxation than RTDs, making it a more profitable prospect for the producer. The growth in the cider market demonstrates the alcohol industry's capacity to quickly adapt to changed taxation arrangements for one product (RTDs) and diversify into products that appeal to a similar consumer market.

Another example of the alcohol industry taking advantage of the incentives under the WET, is the cider industry changing the way they market products. Cider products, as seen with the image below, are now been produced in PET bottles that mimic soft drink and can be purchased for $6.99 for 1.25 litres of apple cider with an eight per cent alcohol content.

These changes within in the cider market is not surprising given the experience in the United Kingdom (UK). Like Australia cider in the UK is given preferential tax treatment, this has led to an increase in cheap cider with high alcohol content. Cider with an alcohol content of 7.5 per cent is as cheap as 20p a unit.[97]

Under a differentiated volumetric taxation system, these products should taxed based on their alcohol content. Cider products, should be taxed using the current beer taxation arrangements, as cider has a similar alcohol content to beer. Where cider has added flavours it should continue to be taxed as a RTD. For products that imitate spirits and have a similar alcohol content these should be taxed at the rate of spirits.

Recommendations

5. That the Tax White Paper Task Force adopt the following policy objectives for Australia's alcohol taxation system:
    i. Alcohol taxation must be applied according to the category and volume of alcohol within products and their potential to cause harm.
    ii. The economic externalities of alcohol consumption must be used to inform alcohol taxation rates.
    iii. Alcohol taxation must minimise distortion that may encourage harmful consumption of alcohol.
    iv. Alcohol taxation must ensure the cost of alcohol increases with average weekly earnings.
    v. Alcohol taxation must minimise loopholes.
    vi. Revenue collected from alcohol taxation should be used to pay for the costs incurred by Governments to address alcohol harms.
6. That the Tax White Paper Task Force recommend removing the ad valorem Wine Equalisation Tax (WET) and replacing it with a volumetric tax rate. This rate should be transitioned to a differentiated rate that is based on the alcohol content of wine.
7. That the Tax White Paper Task Force recommend that the Wine Equalisation Tax (WET) rebate be abolished.
8. That the Tax White Paper Task Force recommend than an industry adjustment package is only necessary to facilitate the need for structural change in the wine industry. This should be independent of the tax system.
9. That the Tax White Paper Task Force tax other products that fall under the Wine Equalisation Tax (WET) at appropriate levels based on their alcohol content, including:
    i. Moving cider to the current beer taxation arrangements, as cider has a similar alcohol content to beer. Where cider has added flavours it should continue to be taxed as a ready-to-drink beverage (RTD).
    ii. Moving 'Spirit' like products to the current spirit tax arrangement, as these products have a higher alcohol content and are marketed as spirits.

Relevant research

Relevant research by FARE in relation to alcohol taxation is described in this section. This research evidence should be referred to by the Tax White Paper Task Force.

FARE has commissioned the following publications which examine the impacts of reforming the alcohol taxation system, copies of each of the below reports are included as Appendices.

- *Bingeing, collateral damage and the benefits and costs of taxing alcohol rationally.* Marsden Jacob Associates (October 2012). Appendix A
- *Alcohol taxation reform: Starting with the wine equalisation tax*. The Allen Consulting Group (September 2011) – Appendix B
- *The liquor industry*. The Australia Institute (August 2012) – Appendix C
- *The Australian wine tax regime: Assessing industry claims*. The Australia Institute (September 2011) – Appendix D

FARE is currently revising some of the modelling referred to in the above papers and will be provided this research to Tax White Paper Task Force when completed.

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