Australian Government

Wine Equalisation Tax Rebate: Tightened Eligibility Criteria

Implementation Paper
September 2016

Context

The Government is putting the wine industry in a stronger long-term position by making a record investment in international and domestic wine promotion, while strengthening wine equalisation tax (WET) integrity rules.

The wine industry has called for reform of the WET rebate based on their concern it has moved beyond its original policy intent, compromising profitability in the wine industry, through:

- the ability to create artificial business structures to access the rebate and claim multiple rebates.
- the conversion of uncommercial grapes into bulk wine for the sole purpose of claiming the rebate, affecting the pricing of both grapes and wine.

In the 2016-17 Budget, the Government announced that it will address integrity concerns with the WET rebate and better target support to small wine producers in rural and regional Australia. In the Budget, the Government announced it would:

- provide $50 million over four years to the Australian Grape and Wine Authority to promote Australian wine overseas and wine tourism within Australia;
- strengthen the associated producer rules in WET legislation to help stop multiple claims for the WET rebate by complex structures of associated businesses;
- from 1 July 2017, reduce the WET rebate cap from $500,000 to $350,000 and from 1 July 2018 to $290,000; and
- from 1 July 2019, apply tightened eligibility criteria where a wine producer must own or lease a winery and sell branded, packaged wine domestically, with final details settled through consultation.

The Government acknowledges the response from the wine industry following the Budget announcement and will work closely with the wine industry to implement reforms to the WET rebate. The Assistant Minister for Agriculture and Water Resources has met with stakeholders in the major wine regions since the Budget announcement to obtain early feedback from the industry. Stakeholders have raised that removing the rebate from bulk and unbranded wine is an important driver to industry’s restructure and would like it to happen as soon as possible. The Government also recognises that the industry utilises a range of wine production models and that production models are changing, such as the increasing incidence of multiple wine producers using central winemaking facilities. Some stakeholders have asked if eligibility can focus on wine producers who own the grapes throughout the manufacturing process and have substantial investment in the wine industry, such as ownership of a winery, vineyard or cellar door.

This implementation paper sets out the Government’s proposed approach to implement the tightened eligibility criteria, giving consideration to these issues. The eligibility criteria would be given effect through the definitions of an ‘eligible producer’ and ‘rebateable wine’ in the WET Act. The Government welcomes the wine industry’s views on the proposed implementation approach.

Tightened WET rebate eligibility criteria

Rebatable wine: Packaged and branded wine

Proposed position: *Packaged wine is wine that is packaged in a container not exceeding 5 litres in a form fit for retail sale. Branded wine is wine that is labelled with a wine producer's trademark.*

A 5 litre limit would capture the overwhelming majority of wine packaged for retail sale and would adopt the recommendations by the Winemakers' Federation of Australia and the WET Rebate Consultative Group. Cider and perry are often sold in 30 litre and up to 51 litre kegs; therefore a 51 litre packaging limit may be more appropriate for these products.

This proposed position could allow both registered and common law trademarks. This would accommodate wine brands in Australia. It could exclude licenced trademarks to prevent exploitation by large retailers which create many trademarks which they then licence out to their subsidiary wine producers.

Eligible producers: Owning or leasing a winery

Proposed position: *A winery is a premise where the quantity of fresh grapes used in the manufacture of wine is not less than 5 tonnes in a year. Definitions of ownership and control could be based on existing tax legislation and leasing requirements could be flexible to accommodate industry practices.*

The proposed position is based on the definition of a winery used for the purposes of the Wine Grapes Levy, contained in the *Primary Industries (Excise) Levies Act 1999*. The definition of manufacture could also be based on the definition used in the same Act which includes all stages of the winemaking process except crushing.

Under the definitions of control and ownership in the income tax law, sole traders meet the ownership test as they have complete control of their business and companies, partnerships and trusts need to hold a 40 per cent interest to meet the control test. The proposed leasing requirement could capture different types of leases used in the wine industry, including sub-leases, multi-year leases and joint leases. A lease may need to be held for at least three years.

However, the wine industry has evolved beyond traditional production methods which would not be recognised under this criterion. The requirement could exclude small wine producers that have a stake in the industry but contract out winemaking for sound economic purposes. A possible alternative approach could be to require a wine producer to retain ownership of the grapes throughout the winemaking process (whether it's made by the wine producer at its own premises or it contracts out the winemaking) and own or lease one of either a winery, vineyard or cellar door.

Further detail

Further detail on the proposed approach to implement the eligibility criteria are in **Appendix A**.

A summary of recommendations that helped inform the Government's decision on WET rebate reform is in **Appendix B**.

Your feedback is important

The Government seeks your comments on the tightened eligibility criteria. The submissions and comments will inform the Government's approach to implementation, and assist it in developing an approach with minimal regulatory burden on industry. The Government will also hold consultation meetings on the implementation arrangements with state and regional wine associations in Adelaide, Melbourne, Hobart, Perth, and Sydney.

Discussion questions

In considering the Government's proposed approach to implementing the tightened eligibility criteria, submitters are urged to have regard to the following discussion questions:

1. For rebatable wine, is the proposed definition of packaged and branded wine appropriate? If a trademark approach is used, what types of trademarks should be permitted (e.g. exclusively licensed trademarks) and what would be the impact?

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

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

Submissions close on 7 October 2016

Submissions close on 7 October 2016.

Please include the name of your organisation (or your name if you are making a submission on your own behalf) and contact details for the submission, including an email address and contact telephone number where available.

Please email responses to wetrebate@treasury.gov.au in a Word or RTF format (for accessibility reasons). An additional PDF version may also be submitted.

All information (including name and address details) contained in submissions will be made available to the public on the Treasury website, unless you indicate that you would like all or part of your submission to remain in confidence. Automatically generated confidentiality statements in emails do not suffice for this purpose. Respondents who would like part or all of their submission to remain in confidence should provide this information marked as such in a separate attachment. A request made under the *Freedom of Information Act 1982* for a submission marked 'confidential' to be made available will be determined in accordance with that Act.

Enquiries can be directed initially to David Pullen, 02 6263 3941

APPENDIX A

Rebatable wine: removing rebates for bulk and unbranded wine

The section provides details on the proposed options to implement eligibility for rebatable wine through the packaged and branded requirements.

Definition of packaged wine

Proposed positon: *Packaged wine is wine that is packaged in a container not exceeding 5L in a form fit for retail sale.*

Details:

The proposed position would adopt the recommendation by WFA to limit the rebate to wine that is packaged in a container with a capacity not exceeding 5L and is in a form fit for retail sale. The WET Rebate Consultative Group also recommended a 5L limit.

Most wine packaged for retail sale would already comply with the proposed 5L requirement. For example, a sampled search of the major online retailers showed that around 99 per cent of their wine products (grape wine) are sold in 750mL bottles or casks up to 5L. Other sizes of packaging for retail sale are very limited, for example there are a few cases of restaurants and pubs that sell wine in kegs which would not comply with any of the above options.

To circumvent the packaging requirement, an entity would need to purchase packaged wine with the packaging costs built in to the price, blend or further manufacture the wine and then repackage the end product, incurring additional costs. The smaller the container size, the more cost prohibitive it would be to unpack, blend or further manufacture and repackage the wine.

The additional element of requiring wine to be in a form fit for retail sale reduces risk of exploitation of the proposed packaging requirement. To comply with this element, wine must be sealed in its final packaging, be labelled in accordance with the requirements under the *Australian Grape and Wine Authority Act 2013* and the Food Standards Code and be labelled with a brand.

These packaging requirements therefore help prevent bulk and unbranded wine sold in large plastic bladders, with some as big as 24,000L, from benefiting from the WET rebate.

Definition of branded wine

Proposed positon: *Branded wine is wine that is labelled with a wine producer's trademark.*

Details:

A brand is a mark, symbol or name which distinguishes a business's product or services from that of its competitors. A trademark is a sign or symbol used to distinguish the goods and services of a business from that of another business.

Trademarks can be registered under the *Trade Marks Act 1995* with IP Australia which provides the owner legal ownership of the mark and exclusive rights to use the mark nationwide. Many Australian wine brands and their sublabels are registered trademarks. Where a wine producer registers a new trademark, it may take around seven months or more from the date of application to the date of registration. This raises the question as to whether the trademark should be recognised from the date of application or the date of registration.

Many wine producers also use common law trademarks instead of registered trademarks. A common law trademark is a mark which has been used in relation to certain goods or services to such an extent that it is recognised as distinguishing the goods or services from other traders. Common law trademarks are less certain than registered trademarks and depend on the mark having developed a reputation in the relevant region by use of the trademark. Many small producers use common law trademarks, but wine producer start-ups are unlikely to have a common law trademark as they would not have developed a reputation in the region. There are also situations where wine brands are unable to be registered as a trademark, for example where they are named after a location, which mean producers need to utilise a common law trademark.

Unlike registered trademarks which can act as a notice that the owner of the trademark owns the rights in a trademark, the only way to have certainty over common law trademark rights is by a judicial or administrative decision.

An additional consideration is whether brands with licensed trademarks would be eligible. A licensed trademark is where a trademark owner (licensor) permits another party (licensee) to use its trademark. WFA and the Consultative Group suggested that the branding restriction include wine labelled with a brand wholly owned by, or licensed exclusively, to the producer of the wine. That is by having the exclusivity requirement; the licence can't be used by several entities which would undermine the concept of a brand. Even with an exclusivity requirement, allowing wine labelled with a licensed trademark would still allow a company, such as a large retailer, to create trademarks to exclusively licence them out to obtain the benefit of the rebate. There may also be an issue of trademarks being exclusively licensed for short time periods and being passed from one entity to another.

Eligible producer: owning or leasing a winery

The section provides details on eligibility for the WET rebate through the requirement to own or lease a winery.

Proposed position: *A winery is a premise where the quantity of fresh grapes used in the manufacture of wine is not less than 5 tonnes in a year. Definitions of ownership and control could be based on existing tax legislation and leasing requirements could be flexible to accommodate industry practices.*

Definition of a winery

In simple terms, a winery is a place where wine is made. The wine making process entails a number of major steps, including crushing and pressing, fermentation, clarification, aging and packaging.

There is already a legislated definition of a winery used for the Wine Grapes Levy, contained in the *Primary Industries (Excise) Levies Act 1999*. This Act defines a premise as a winery if the quantity of fresh grapes or fresh grape equivalent (of dried grapes, grape juice and/or concentrated grape juice) used in the manufacture of wine at those premises during that year, or either of the immediately preceding two years, amounts, or amounted, to not less than 5 tonnes. Grapes and grape juice are taken to have been used in the manufacture of wine if they are subjected to any wine making process (excluding crushing and the concentration of grape juice), whether or not that process or any other wine making process is completed.

This legislative definition is quite broad — while it excludes crushing, it would include packaging. It also includes manufacturing brandy as part of the wine making process, which would need to be excluded as it is subject to the excise system. The separate packaging requirement to access the WET rebate deals with the final stages of the wine making process and it may be appropriate to exclude this step from the definition of the wine making process for the purposes of defining a winery. Under this approach, a premise where fermentation, clarification, blending or aging occurs would be deemed to be a winery subject to the 5 tonne requirement.

An alternative way of defining a winery is by reference to assets as a winery will need to possess certain equipment such as tanks and barrels to undertake the wine making process. Adopting this approach would require a detailed specification of physical assets as well as determining issues such as the appropriate size and numbers before a premise can be deemed a winery.

Definition of owning and leasing

Once it is established that a place is a winery, the second stage involves determining whether an entity owns or holds a long term lease over the winery. This requirement is intended to ensure that those that claim the WET rebate have a tangible investment in the wine industry.

Ownership structures vary depending on the circumstances and different ownership structures are warranted for differing reasons. A winery could be owned by a partnership, a cooperative, or a company. The proposal would rely on definitions of control and ownership already contained in existing legislation. In the case of a sole trader owning a winery, as the sole trader has complete control over the management and direction of its business, it will meet the ownership test. In the case of a company, partnership or trust the existing income tax legislation, in general, specifies a 40 per cent holding/interest is required to meet the control test.

The proposed position would use these existing definitions, which taxpayers may already be familiar with, rather than attempt to introduce new concepts of control in the WET Act. The proposed position could also capture the different types of leases provided they reflect normal arm's length (commercial) business conditions to allow flexibility but also ensure the integrity of this requirement. For example, a winemaker might sub-lease the winery if they do not need to fully use the winery they are leasing. Another example is a multi-year lease that allows the winemaker to use the winery for a few weeks a year at the time they harvest their vintage. There may also be cases of multiple leases or joint leases, such as a large winery accommodating multiple winemakers in their region using the winery at one time or through different points in the year.

Under the leasing requirement, however, there may be a temptation for some businesses to try and circumvent the requirement. For example, a wine producer might enter into a long term lease (rather than a shorter lease) with the sole purpose of claiming the rebate and terminate the lease early. Dealing with such instances through specific anti-avoidance rules would introduce additional complexity to the tax law. Instead, an approach that could be adopted is for the onus of proof to be on the entity to show that the activity was on a commercial basis and not simply to just access the rebate.

For the length of the lease, a minimum three year period could be used to satisfy the interest in a winery test. However, a longer lease period may be appropriate. Leases entered into before 1 July 2019, that continue to apply after 1 July 2019 could be given the same treatment, that is, the particular lease would need to meet the minimum yearly requirement to be eligible for the rebate. The lease would need to cover the winery—or part of the winery—itself, and does not include contracting out the winemaking service.

Significant interest in a winery or significant investment in the wine making industry

The Government recognises that there is a range of wine production models in the industry, including grape growers who have a real investment in the wine making industry, but may not own equipment for manufacturing wine. By introducing an ownership or leasing test over a winery, this could exclude those that might be normally considered to have a stake in the wine making industry, which could be argued is contrary to the policy intent of providing access to the WET rebate to those that have an investment in the wine making industry.

A less stringent requirement compared to owning or holding a long term lease over a winery could be that an entity would need to have a significant interest in a winery or in the wine making industry. While this approach is consistent with the policy objective, a significant interest test may be difficult to implement and administer and could easily be circumvented.

There have been various views expressed on what would constitute a significant interest but no unanimous view has been reached. The main suggestions have included: ownership of wine making equipment, business premises, regional employment, regional business investments, local liquor licences, cellar door, vineyard ownership, and investment in wine making education (such as university qualifications).

In the Consultative Group's report on the Wine Equalisation Tax Rebate of October 2015, there was a recommendation that as part of amending the definition of a wine producer, an entity would need to own or lease one out of three of a vineyard; winery (production facilities or fermentation facilities); or cellar door outlet. However, as noted in the report, there was some divergence in views held about the 'one out of three' test and that a 'two out of three' test should be preferred.

A threshold question in the context of defining a significant interest test is what and how many of these tests will need to be met before an entity is deemed to have a significant interest. The issues with defining a winery by reference to its physical assets are equally relevant in the context of developing a significant interest test, which would require decisions around size and scope.

It is important to keep in mind that the Government wants to avoid increasing the complexity of the tax law, in line with its broader objective for tax policy.

A possible alternative approach could be to require a wine producer to retain ownership of the grapes throughout the winemaking process (whether it's made by the wine producer at its own premises or it contracts out the winemaking) and own or lease one of either a winery, vineyard or cellar door. If such an approach is adopted, there would also be a need to define vineyard and cellar door.

Cider, perry, mead, sake, fruit and vegetable wine, and grape wine products

Cider, perry, mead, sake, fruit and vegetable wine, and grape wine products are all defined as 'wine' under the WET Act and are eligible for the WET rebate. The proposed options will be amended to cater to the circumstances of the industry.

- In terms of the winery definition, it is proposed that the principles that apply to a winery should extend to entities that produce these other wine products. However, the 5 tonne requirement may not be suitable for all other wine products, and may need to be adjusted.

- In terms of the packaging requirements, it is proposed that cider and perry must be packaged in a container not exceeding 51L in a form fit for retail sale. This is a reflection that cider and perry are often sold in 30L and up to 51L kegs to provide sales on tap at pubs.

APPENDIX B

Previous reviews and recommendations

The WET rebate reforms deliver savings to the Budget and are informed by policy positions put forward by industry and through formal processes. These include the Winemaker's Federation of Australia Pre-budget Submissions (2015 and 2016), the Government's 2015 Discussion Paper and WET Rebate Consultative Group report (2015), and the Senate Rural and Regional Affairs and Transport (RRAT) Committee inquiry into the Australian grape and wine industry (2015). A summary of the recommendations follows:

Measure	Recommending Group	Recommendation
Definition of Eligible Producer	Winemaker's Federation of Australia	Producer must: • have business premises in Australia (potentially, in a designated wine region in Australia); and • hold a licence, issued by the Government of a state or territory in Australia, to sell liquor in that state or territory; and • are self-employed or engage one or more employees (including associates of the winemaker) to perform work for the winemaker; and • sell their wine either: - by retail sale, or under quotation, from the business premises referred to above; or - by internet or mail order sales (in which case the sales would be deemed to take place at the above premises).
	WET Rebate Consultative Group	Aligns with the Winemaker's Federation of Australia definition, but also includes an asset test which requires a producer to own or lease 'one out of three' of a vineyard, winery or cellar door.
	Senate Committee	Phase out the WET rebate and transition to a grant scheme.
Government position	Budget 2016-17	Producer must own or lease a winery
Definition of Rebatable Wine (Removal of Bulk & Unbranded)	Winemaker's Federation of Australia	Wine that is packaged in a single container not greater than 5L and is labelled with a brand wholly owned by or licenced exclusively to the producer.
	WET Rebate Consultative Group	Wine that is packaged in a single container not greater than 5L and is labelled with a brand wholly owned by or licenced exclusively to the producer.
Government position	Budget 2016-17	Wine that is packaged, branded and sold domestically.
Alterations to WET Cap	Winemaker's Federation of Australia	Wet rebate cap remain at $500,000.
	WET Consultative Group	Wet rebate cap remain at $500,000.
	Senate RRAT Committee	Phase out the WET rebate and transition to a grant scheme.
Government position	Budget 2016-17	WET rebate cap reduced to $350,000 from 1 July 2017 and to $290,000 from 1 July 2018.
Industry assistance for International Marketing	Winemaker's Federation of Australia	$43.4m for Wine Australia.
	WET Consultative Group	Funding for Wine Australia and EMDG Programs
	Senate Committee	Increase funds for Export market development
Government position	Budget 2016-17	$50m for Wine Australia.