TTB BOND AND EXCISE TAX REPORTING CHANGES: COMING IN 2017

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Davis Wright Tremaine LLP is a full service law firm providing services to the wine industry in the areas of mergers and acquisitions and other business transactions, land use and real estate, alcohol regulatory and licensing, intellectual property, employment, and litigation.

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The PATH Act ("Protecting Americans from Tax Hikes" Act) will be effective on Jan. 1, 2017. Important changes affecting the alcohol industry include amendments to excise tax-return deadlines, a new exemption from bond requirements for certain alcohol producers, and a broader definition of "hard cider" for tax-rate classification purposes. Keep in mind, current TTB rules must be followed through Dec. 31, 2016.

SUMMARY OF CHANGES TO TAKE EFFECT ON JANUARY 1, 2017:

1. Excise taxes may be paid annually, rather than quarterly, for wineries, breweries, and distilled spirits plants (DSP) that owe <$1,000 excise tax/year.
2. No bond will be required for wineries, breweries and DSPs that qualify to pay taxes <u>annually</u> (<$1,000/year) or <u>quarterly</u> (<$50,000/year).
3. Cider definition will be broadened to include: (a) an increase allowable alcohol content; (b) an increase in allowable carbonation; and (c) allowed use of pears as well as apples. Note: Cider labeling will not be affected, just the definition for tax-rate classification purposes.

THE DETAILS:

1. **<u>Change to TTB Excise Tax Due Dates: Annual Tax Returns if <$1,000/year liability</u>**. Producers of wine, beer and distilled spirits who pay (or who reasonably expect to be liable for) $1,000 or less per year in excise tax to TTB will be able to pay excise taxes annually, rather than quarterly or semimonthly. (*Note*: Wineries paying $1,000 or less per year in excise taxes may already pay annually, but as of Jan. 1, 2017, annual filing will also be extended to qualifying DSPs and breweries).

2. **<u>Change to Bond Requirement: Bond Exemption for Annual and Quarterly TTB Excise Tax Return Filers</u>**. Currently TTB requires a bond for a minimum of $1,000 for wineries and breweries, and $5,000 per operation for DSPs ($5,000 each for distilling, processing and warehousing, so typically a $15,000 bond).

   As of Jan. 1, 2017, wineries, breweries, and distilleries that qualify to file annually (pay <$1,000 excise tax/year) or quarterly (pay <$50,000 excise tax/year) will be <u>exempt</u> from the bond requirement. It is estimated that this will exempt the majority of Oregon and Washington state wineries from the TTB bond requirement.

   As an example, an Oregon winery that produces 50,000 gallons of 13.5% ABV wine per year and removes all of it from bond for sale in Oregon would have an excise tax liability to TTB for $8,500 (50,000 gallons x $0.17/gallon as a small producer). As of Jan. 1, 2017, this winery would continue to file TTB excise taxes quarterly, but would no longer need a bond.

   TTB is formulating guidance now for the refund process for qualifying permittees who have paid a cash bond and who will no longer be required to have a bond under the new requirements. DWT should send a notice to OWA members and our brewery and distillery clients about the upcoming bond exemption.

   Also note that in Oregon, wineries that do not owe OLCC privilege tax (produce <100,000 gallons/year, and sell <40,000 gallons/year in Oregon) are also currently exempt from a separate OLCC bond requirement. Such a winery must file an OLCC bond-waiver form before being licensed, or before their license renewal is due. But the new TTB bond waiver is automatic; no waiver form is required.

3. **<u>Change to Definition of "Hard Cider" for Cider Tax Rate</u>**. Currently, "hard cider" is defined as a "still wine derived primarily from apples or apple concentrate and water, containing no other fruit product, and containing at least 0.5% and no more than 7% ABV." Since the definition of hard cider states that the wine must be "still," cider cannot exceed 0.392 grams of carbon dioxide per 100ml. The existing definition of hard cider also excludes perry, which is wine made from pears.

   The alcohol content of many wines made from cider apples can be high, so ciders with >7% alcohol and/or higher levels of effervescence do not meet the current hard-cider definition for tax-rate classification purposes.

Hard cider is taxed at the low rate of 22.6 cents/gallon (17 cents/gallon for small producers). In contrast, still table wine under 14.1% ABV is taxed at $1.07/gallon tax rate on wines (less for small producer credit). For sparkling wine, the tax rate is $3.40/gallon on naturally sparkling wines (no small producer credit), and $3.30/gallon tax on artificially carbonated wines.

As a result, some cider producers that run close to these limits may dilute their cider with water and/or reduce the amount of carbon dioxide (fizziness) in order to qualify for the more favorable hard-cider tax rate.

The PATH Act amends the definition of wine that is eligible for the more favorable "hard cider" tax rate by increasing the allowable alcohol content from <7% to <8.5% ABV; increasing the allowable carbonation level from 0.392 to 0.64 gram of carbon dioxide per 100ml of wine; and authorizing the use of pears, pear juice concentrate and pear products and flavorings. With the increased alcohol content and carbonation that will be allowed as of Jan. 1, 2017, more cider manufacturers' products will qualify for the lower tax rate. Note that this new definition will only apply to tax rates, not to labeling, advertising or permitting requirements for cider.

In summary, as of Jan. 1, 2017, the definition of "hard cider" for tax-rate purposes will be wine that:

- Contains no more than 0.64 grams of carbon dioxide per 100ml;
- Made from apples, pears, or concentrate of apples or pears and water;
- Contains no other fruit product or fruit flavoring other than apple or pear; and
- Contains ≥0.5% and <8.5% ABV.

For more information, see TTB advisory on the PATH Act changes here: http://www.ttb.gov/announcements/ttb-announcement-cider-statutory-changes.pdf.

DISCLAIMER

STILL HAVE QUESTIONS? CONTACT THE OREGON WINEGROWERS ASSOCIATION, 503.228.8336, OWA@OREGONWINE.ORG