Dissenting report of Senator Nick Xenophon

The Wrath of Grapes

Enough is enough

1.1 The Australian wine industry, including grape growers and wine producers, faces an existential crisis.

1.2 Successive Winemakers' Federation of Australia (WFA) Vintage Reports have set out the parlous state of an industry that is both iconic and the economic lifeblood of regional communities around the nation.

1.3 As noted in the report, a mismatch of supply and demand has been accompanied by falling profits for wine makers. By 2014, an estimated 84 per cent of producers were not covering their variable costs, up from 77 per cent in 2012. This is in stark contrast to the United States and New Zealand producers receiving positive returns over the past six years.

1.4 The WFA estimates that up to 70 per cent of total current Australian wine and grape production maybe uneconomic. Further, the WFA Vintage Reports in recent years paint an even bleaker picture, particularly for the warmer inland regions. These regions, including the Riverland, Sunraysia and Riverina have been hit hard by a perfect storm of factors that have driven up to 90 per cent of the industry in those regions into unprofitability.

1.5 The dithering of successive Governments over the unintended consequences of the WET rebate scheme, an anaemic export push for Australian wine, and the supermarket duopoly have all hit the sector hard.

1.6 The inquiry, which I co-sponsored with my colleague Senator the Hon Anne Ruston, now the Assistant Minister for Agriculture and Water Resources, was a critical opportunity to set out in a non-partisan manner the scope of the problems facing the sector, the urgent need for reform, and above all a pathway for recovery and renaissance of this great industry.

1.7 Tragically, the opportunity to set out an urgent pathway forward has been lost, with some of the key recommendations of the report failing, in my view, to reflect the weight and gravity of the evidence presented.

1.8 It appears that obvious, sensible, measured recommendations for reform and recovery have been ignored.

1.9 The great fear I have is that the views of the major parties expressed through this committee will give cover to the Government to either avoid taking urgent remedial action now, or worse, pursue options that will hasten the demise of many hundreds of family enterprises, whether grape growers or wine producers.

1.10 Putting the squeeze on these smaller and medium players will mean an incalculable diminution and loss of social and entrepreneurial capital amongst grape growers and wine makers, profoundly impacting on regional communities and their economies. In turn, the forced consolidation this will bring will mean a loss of diversity and vibrancy in this iconic industry.

1.11 I commend the committee in the consultative and fair way this inquiry was conducted and the professionalism of the secretariat. The submissions obtained, the evidence heard and the summary of the evidence in the report has been a most useful exercise. I take issue with some of the recommendations which, in my view, are fundamentally at odds with the weight of evidence presented to the inquiry.

Wrong Way, Go Back

1.12 The report's first recommendation is as follows:

> The committee recommends that the Government phase out the current Wine Equalisation Tax (WET) rebate over five years, allocating the savings to a structural adjustment assistance program for the industry including an ongoing grant to genuine cellar door operators to support their continued operation.

1.13 Respectfully, this recommendation is misconceived, goes against the weight of the evidence, and is dangerously counterproductive.

1.14 The weight of the evidence provided to the inquiry is set out in the report. It includes the glaring apparent problems with the WET rebate including;

- Morphing way beyond its original purpose to deliver long term benefits to industry, assist smaller wine makers and boost tourism in regional Australia;
- The anomalous WET rebate for New Zealand wine producers, costing between $25 million and $35 million per year. This, in effect, subsidises New Zealand wine makers with our money to undercut and hurt Australian wine makers and grape growers;
- Evidence of wide spread rorting that occurs, the multiple-transactions, the deals done on bulk and unbranded wine, all of which were never intended when the scheme was established; and
- These negative effects include pushing the price of wine grapes down, putting smaller wineries under unfair pressure, and consolidating the power of large retailers.

1.15 The reform proposal presented by key industry players, led by the WFA, were measured, sensible and urgently needed. In summary these proposal are to:

- Keep the WET rebate in line with the original policy intent of delivering long-term benefits to industry and tourism in regional Australia;
- Stop the rebate going to unintended recipients and shut down the schemes;

- Phase out the WET rebate on bulk and unbranded wine over four years to advance strong brands that command consumer loyalty and profitable margins to reinvest back into regional Australia;
- Abolish the separate New Zealand rebate arrangements that provide preferential treatment to NZ wine producers and replace it with a level playing field for all claimants, irrespective of nationality;
- Encourage winery consolidation, where appropriate, by introducing transitional WET rebate measures that allow the separate rebate entitlements of the merging entities to be phased down to one entitlement over four years;
- Return $44m of government savings from these reforms to industry to boost marketing of Australian wine to grow export demand; and
- Provide industry support to assist those impacted by the changes.

1.16 The WFA has conservatively estimated that their plan would have delivered net savings to the Commonwealth of at least $234 million over the next four years. My principal criticism of the WFA proposal was that the $44 million proposed for marketing may not be enough given we have a lot of catching up to do in building up world export markets.

1.17 These above proposals were in effect, initially put to then Treasurer Joe Hockey and to Assistant Treasurer the Hon Josh Frydenberg MP. The parlous state of the sector and representations across a broad sector of industry was the impetus for the Treasury's WET rebate discussion paper, which, after seemingly unnecessary delay was released in August 2015.

1.18 The discussion paper spelt out the problems with the rebate, including the rorting (with a virtual ‘how to’ guide as to ways to rort the system) and made a compelling case for reform.

1.19 Inexplicably, the Government is yet to announce its reform package despite the palpable urgency of the situation. Harvest has already started and it may well be the last harvest for an increasing number of wine grape growers.

1.20 The brutal reality is that there are increasing parts of Australia’s iconic wine sector that are struggling to survive.

1.21 The apparent increase in wine and grape prices compared to last year’s vintage harvest mask the increased cost of production since then – especially water.

1.22 To suggest, as the report does, that the WET rebate be phased out and replaced with a specific grants program for some smaller wineries is throwing the baby out with the bath water.

1.23 The most credible pathway to reform is that set out by the WFA and other key stakeholders. It was a broad consensus position reached that is fairer and more effective than any other proposals put to the committee.

1.24 Exports are the key to dealing with the supply demand imbalance.

1.25 Now is the time to seize the opportunity with the lower Australian dollar and recently negotiated free trade agreements to turbo-charge our sales of Australian wines to the world (although I am a trenchant critic of many clauses in free trade agreements, particularly their impact on our manufacturing sector, I acknowledge there is an upside for wine exports to some markets).

1.26 Australia's efforts to showcase, promote and sell Australian wine to world has been largely anaemic. Our lack of appropriate presence in international wine expos and trade shows has been largely embarrassing.

1.27 Our competitors have left us for dead in terms of their marketing push and results for their producers.

1.28 I make the following recommendations:

Recommendation 1

1.29 Keep the WET rebate in line with the original policy intent of delivering long-term benefits to industry and tourism in regional Australia;

Recommendation 2

1.30 Stop the rebate going to unintended recipients and shut down the schemes;

Recommendation 3

1.31 Phase out the WET rebate on bulk and unbranded wine over four years to advance strong brands that command consumer loyalty and profitable margins to reinvest back into regional Australia;

Recommendation 4

1.32 Abolish the separate New Zealand rebate arrangements that provide preferential treatment to NZ wine producers and replace it with a level playing field for all claimants, irrespective of nationality;

Recommendation 5

1.33 Encourage winery consolidation, where appropriate, by introducing transitional WET rebate measures that allow the separate rebate entitlements of the merging entities to be phased down to one entitlement over four years;

Recommendation 6

1.34 Return $44m of government savings from these reforms to industry to boost marketing of Australian wine to grow export demand.

Recommendation 7

1.35 Provide industry support to assist those impacted by the changes.

Going Down, Down, Down – The Effect of the Duopoly on the Wine Retail Sector

1.36 Chapter 3 of the report fairly sets out the concentration of the Coles/Woolworths duopoly in a domestic wine retail market of 60 per cent, and the increasing push for private brands.

1.37 The private brands push unambiguously puts ‘further price and margin strain on growers and wine producers alike’ according to the Australian Small Business Commission. With private brand sales going from an estimated 5 per cent in 2005 to up to 20-25 per cent now, this is a disturbing trend.

1.38 I support the report's recommendation that the Government amend labelling requirement so that wine labels must declare where the wine is produced by an entity owned or controlled by a major retailer.

1.39 But we need to go further to allow small wine makers to grow and flourish. A strong effects test in our competition laws is needed to ensure abuses of market power do not occur. That test should not be fettered by the ‘substantial lessening of competition’ proviso as set out in the Harper Review.

1.40 Further, having divestiture powers in our competition laws as I proposed in the Competition and Consumer Amendment (Misuse of Market Power) Bill 2014 would lead to a change of culture or behaviour amongst some larger corporation in the way that they deal with smaller companies.

1.41 In addition, the codes of practice need to be overhauled and strengthen to give a real right of redress to growers and wine producers alike.

Recommendation 8

1.42 I recommend an effects test in respect of abuses of market power.

Recommendation 9

1.43 I recommend divestiture laws as a penalty in cases of abuse of market power.

Recommendation 10

1.44 I recommend an overhauled and strengthened mandatory code of practice to provide protection to growers and wine makers from unconscionable practices and abuses of market power.

Senator Nick Xenophon
Senator for South Australia