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ALCOHOL AND TOBACCO TAX DIVISION



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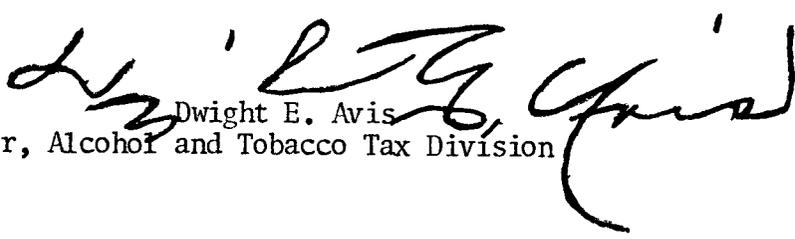
LIQUOR LAW REVISION PROGRAM

Proprietors of distilled spirits
plants, bonded wine cellars, and
others concerned:

At the annual meeting of the National Conference of State Liquor Administrators in Louisville, Kentucky, on June 10, 1963, I discussed some of the key elements of a series of proposed revisions of law as developed by our Liquor Law Revision Committee. At that time industry cooperation was solicited and suggestions were invited with respect to the Committee plan to further simplify and modernize our system of liquor tax administration. Copies of the Louisville remarks were made available to members of industry, industry associations and trade publications.

In view of the controversy which arose over any prospective change in the wine gallon-proof gallon taxing provisions of Section 5001(a)(1), I.R.C., the Committee has now developed a modified proposal which retains many of the advantages of its "all-in-bond" recommendation, but which would avoid any change as to the status quo of taxing imported distilled spirits.

The Committee proposals are attached for your study. Your comments are invited so that we may further evaluate the operating aspects of these proposals, and have the benefit of industry reaction by the end of the year. Comments should be addressed to the Director, Alcohol and Tobacco Tax Division (CP:AT:PBF), Washington, D. C. 20224.


Dwight E. Avis
Director, Alcohol and Tobacco Tax Division

Attachment

TREASURY DEPARTMENT
Internal Revenue Service
Alcohol and Tobacco Tax Division
Washington, D.C. 20224

September 27, 1963

TO: Mr. Avis

FROM: Liquor Law Revision Committee

SUBJECT: Proposals for Changes in Liquor Tax Administration

Some of the more significant features of a series of proposals by the Liquor Law Revision Committee to further simplify and modernize our system of liquor tax administration were made known by you to the industry last June in Louisville. The first proposal was the all-in-bond concept in which all operations now performed on bottling premises would be performed prior to determination of tax on bonded premises with the tax to be determined and collected on the proof gallon of the bottled product at the time of withdrawal of the cased goods. This proposal contemplated a change in the taxing effect of Section 5001(a)(1), I.R.C.

The second proposal was to eliminate the tax differential effects incident to the use of wine and alcoholic flavors subject to drawback when blended with distilled spirits, which would achieve a single uniform tax on all products sold as distilled spirits. The third and last proposal made known at Louisville was the elimination of the rectification tax.

Many other proposals beneficial to Government and industry were contained in the Committee's original plan. However, only the above three enumerated proposals, which formed the core of the suggestions, were made known at that time in order to solicit industry reaction, and to provide industry with an opportunity to reconcile its differences so a legislative package could be developed which would be reasonably equitable and generally acceptable.

Adverse industry reaction to these proposals was primarily directed to the first proposal. In recognition of this reaction, the Liquor Law Revision Committee has now developed an outline of a new proposal which would avoid any change in the provisions of Section 5001(a)(1), I.R.C., and thereby maintain the status quo on taxing imports. In order to retain as much as possible of the original all-in-bond plan, the first step in developing the new proposal was to reduce to a minimum the operations which would need to be conducted out of bond. It was found that the bonded premises could be extended to include most of the processing activities presently conducted on bottling premises. A brief outline of the proposal follows:

Bonded Premises Operations

1. Production

All distillation and redistillation, including redistillation now conducted on bottling premises, would be performed on bonded premises. Redistillation of spirits would be considered new production, including the production of gin or vodka by redistillation of neutral spirits. The manufacture of vodka by other approved processes subsequent to production gauge of neutral spirits would be treated as "processing in storage" and thus would not need to be produced in a closed system. There would be no production of gin or vodka on bottling premises.

2. Storage

No change is contemplated in the 20-year bonding period. Spirits in storage could be processed prior to removal from bond as described in Paragraph 3. Processing in storage means (1) the final complete preparation, including bottling and casing or packaging, of distilled spirits products which are bottled in bond or bottled for export and which could remain in bonded storage, (2) the manufacture of vodka by processes other than redistillation, and (3) the preparatory steps in the manufacture of distilled spirits products which are to be tax determined and removed promptly to bottling premises for completion.

Except for spirits to be bottled under Section 5233, I.R.C., (bottling in bond), restrictions under the Code as to the mingling of spirits for further bulk storage would be eliminated. Any such liberalization would necessitate the revision of FAA regulations in order to realize the full benefits of the Code revisions. Mingling in bonded storage would differ from processing in bonded storage in that (1) spirits after mingling would be retained for further bonded storage in bulk containers, and (2) blenders, wines, etc., could not be added during the mingling. Spirits which differ in age and which are mingled for further storage would assume the age of the youngest for purposes of the 20-year bonding limitation.

Imported spirits of any proof could be entered into internal revenue bond in bulk containers (five wine gallons or more) and the force out date would start to run from day of deposit for spirits of less than 190 proof. The importer would be required to pay duty at time of withdrawal from customs; customs would not collect the internal revenue tax on such spirits entered into internal revenue bond.

3. Processing in Storage

Products would be blended or manufactured to the extent possible in bond. All alcoholic ingredients (including drawback flavors and

wines) would be combined in bond prior to tax determination. Nonalcoholic ingredients (juices, oils, color, sugar, etc.) could be added, at the discretion of the proprietor, either on bonded premises during processing or on bottling premises after tax determination. However, to avoid taxpayment on a wine gallon basis, products would need to be 100 proof or higher at time of tax determination. For some proprietors processing in bond would require changes from present processing procedures or the development of new processing procedures.

The following products processed in storage would be eligible for transfer in bond: (1) spirits to be returned to production for redistillation, (2) vodka produced by charcoal or carbon treatment in processing, (3) bottled-in-bond spirits, and (4) products intended for export. All other products processed in storage would be required to be tax determined and withdrawn to the processor's contiguous bottling premises.

Wine required for use in distilled spirits products would be transferred in bond from wineries or customs to distilled spirits plants. Alcoholic blenders or flavors (drawback alcohol) would also be deposited in bond and the proprietor would be authorized to file claim for credit to be taken on future tax returns as to the difference between the tax paid on the blenders and the amount claimed for drawback. (The processing of wine products would be authorized only in bonded wineries or bonded wine cellars. Alternation of bottling equipment between distilled spirits plant and winery premises would be authorized.)

The present requirements for bottling in bond under the provisions of Section 5233, I.R.C., would be retained. Spirits bottled on bonded premises for export but not bottled under Section 5233, I.R.C., could not be labeled in any manner which might indicate that they were bottled in bond.

Any spirits withdrawn on tax determination on or after the effective date of the change-over could be returned to bonded premises for reprocessing, redistillation, denaturation, or destruction with internal revenue tax refund or credit allowed on such returned spirits; such spirits merely requiring relabeling and restamping would be returned to the bottling premises.

Bottling Premises Operations

1. General

All bottling house proprietors would be required to maintain bonded storage facilities (including tax determination facilities) sufficient for their needs.

After addition of nonalcoholic ingredients (if any), reduction, and completion of bottling, the losses incurred and completions achieved would be determined and balanced against the related tax-determination gauge. Losses as established would be entered on taxpayment records and paid on the return for the period in which incurred; any gains in bottling would be deducted from the losses for taxpayment purposes. Transfer of cases to another bottling premises prior to taxpayment would not be permitted. All cases would be taxpaid on the return for the period in which they were removed from the bottling premises, and within six months of tax determination of the spirits.

2. Losses

The record of completions would establish losses (tax determination less completions) by tax-determined lots, and gains would also be a matter of record. Net losses for a claim period would be allowable for credit or refund under Section 5008(c), I.R.C. Future experience probably would indicate the necessity for revising, by regulations, the schedule of allowances.

3. Case Accounts

The proprietor would be required to make and record promptly an accurate count of completions, associating the cases by date, serial number, and/or other identifying marks, with the bottling record and tax-determination record. A complete and strict accounting for all completions would be required, with no losses allowed thereafter.

Taxpayment Based on Removals from Bottling House

1. Records

Accounting for case goods would be on the basis of lots, established by the bottling records related to the appropriate tax-determination records. Removals of case goods from the bottling house would be recorded promptly and a record so maintained as to reflect currently at all times the stock of case goods remaining in each lot.

2. Case Goods in Bottling House

Case goods retained after bottling would be so floored as to permit removal, and taking of inventories, by lots. Tax-determined goods on which the tax had been paid would be removed from the bottling house or segregated from goods on which the tax had not yet been paid.

3. Tax Returns

Tax returns, with payment, would be filed semi-monthly to cover --

- (a) All losses sustained in the bottling house prior to completion of bottling,
- (b) All case goods removed from the bottling house,
- (c) All case goods tax determined six months previously and still on hand, and
- (d) All shortages found in tax-determined case goods,

during the return period. The tax would be paid on the proof gallons represented.

4. Retention of Spirits

Any goods remaining in the bottling house six months after tax determination would be included in the return for the return period in which the final day of the six months' period fell.

Advantages

The above proposal would -

1. Provide for payment of tax on the removal of the case goods from the bottling premises where bottled subject to a six-months' limitation.
2. Make uniform the tax rate on alcoholic content of products by
 - a. Repeal of the rectification tax, and
 - b. Elimination of the tax advantages through use of wines and blenders.
3. Provide for more flexibility and freedom of action by proprietors in the preparation of their products and in the conduct of operations.
4. Simplify overall tax administration.
5. Permit orderly scheduling of bottling operations.
6. Simplify taxpayment of bulk imports with the Internal Revenue Service the only agency involved.
7. Simplify bottling loss considerations.
8. Permit exportation, without payment of tax, of products, including blended whiskies, cordials, etc., without establishing separate customs manufacturing bonded warehousing facilities to conduct such operations.