



Section 5010 Tax Credits for Distilled Spirits

**Presented by
Dave Bateman, Karl Joedicke, and
Dr. Jeff Ammann**



5/2008

5010 Tax Credit Qualification

**Dave Bateman,
Distilled Spirits Industry
Analyst**



How to Qualify for 5010 Credits

- Have a Federal Alcohol Administration (FAA) Act permit as a distilled spirits plant (DSP) or importer
- Have a formula using wine and alcoholic flavorings
- Keep a batch record of spirits made with wine and alcoholic flavorings

Alcohol and Tobacco Tax and Trade Bureau



Flavorings

- **27 CFR 19.374, Manufacture of nonbeverage products, intermediate products, or eligible flavors**
 - Distilled spirits and wine may be used for the manufacture of flavors or flavoring extracts of a nonbeverage nature as intermediate products to be used exclusively in the manufacture of other distilled spirits products on bonded premises.
 - Nonbeverage products on which drawback will be claimed, as provided in 26 U.S.C. 5131-5134, may not be manufactured on bonded premises.

Alcohol and Tobacco Tax and Trade Bureau



Flavorings (Cont'd)

- Premises used for the manufacture of nonbeverage products on which drawback will be claimed must be separated from bonded premises.
- For purposes of computing an effective tax rate, flavors manufactured on either the bonded or general premises of a distilled spirits plant are not eligible flavors.

Alcohol and Tobacco Tax and Trade Bureau



Alternating Premises

- **27 CFR 19.206, Curtailment and extension of plant premises for the manufacture of eligible flavors**
 - **General.** The premises of a DSP may be alternately curtailed and extended, as provided in this section, to permit the use of the facilities for the manufacture of eligible flavors.

Alcohol and Tobacco Tax and Trade Bureau



Alternating Premises (Cont'd)

- **Qualifying documents.** When a portion of the DSP premises is first to be curtailed or extended as provided in this section, the proprietor shall file with the regional director (compliance):
 - An application for registration, TTB Form 5110.41, to cover alternate extension and curtailment of the premises, and
 - A special diagram, in duplicate, delineating the premises as they will exist, both during extension and curtailment, and clearly depicting all buildings, floors, rooms, areas, equipment and spirits lines (identified individually by letter or number) which are to be subject to alternation, in their relative operating sequence.

Alcohol and Tobacco Tax and Trade Bureau



Alternating Premises (Cont'd)

- **Proprietor's responsibility.** Once such qualifying documents have been approved, the designated premises and equipment may be alternately curtailed or extended pursuant to notice on TTB Form 5110.34.
 - **Bonded spirits** on portions of bonded premises that are to be curtailed need not be removed if the spirits are taxpaid concurrent with the filing of TTB Form 5110.34 to effect curtailment; and
 - **Taxpaid spirits** which are on portions of premises to be included by extension of bonded premises and which have not been used in the manufacture of a nonbeverage product need not be removed if the spirits are to be dumped immediately and returned to bond under the provisions of subpart U of this part.

Alcohol and Tobacco Tax and Trade Bureau

5010 Credit Computation



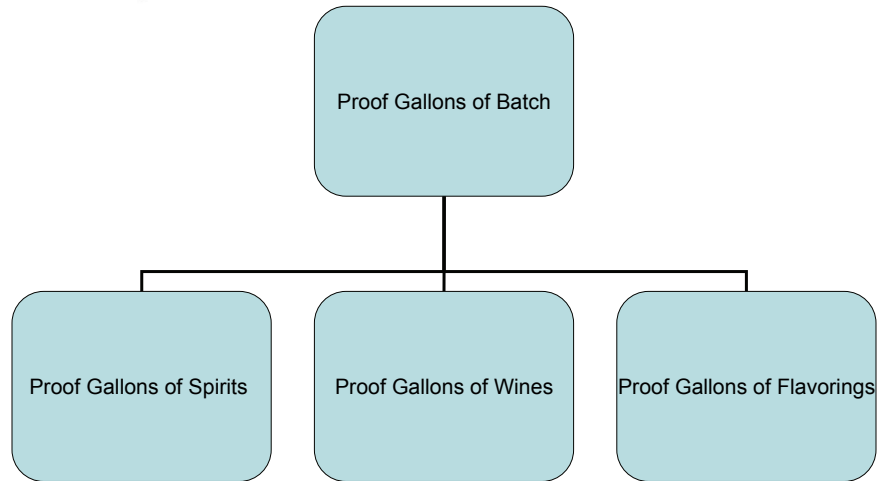
5010 Tax Credit

- Credit for eligible flavors used in approved formulas and/or wines in the processing of distilled spirits.

Alcohol and Tobacco Tax and Trade Bureau



Composition of Approved Formula



Alcohol and Tobacco Tax and Trade Bureau



5010 Credit Computation

EXCISE TAX LIABILITIES (\$)

PROOF GALLONS OF ALCOHOL IN BATCH

Alcohol and Tobacco Tax and Trade Bureau



5010 Credit Computation (Cont'd)

DISTILLED SPIRITS + WINES (Listed By Class)
+ FLAVORINGS (Exceeding 2.5%)

**(W.G. Spirits *Proof) + ((W.G. Wine * % alcohol)*2) +
(W.G. Flavors [2.5% limit does not apply]* Proof)**

Alcohol and Tobacco Tax and Trade Bureau



Tax Advantage

- Allows for alcohol content of 2.5% of batch to be tax exempt
- Taxes alcohol content of wine at the lower wine tax rate
- Can be listed in proprietors records as a total credit of a reduction from the tax rate
 - \$13.50 – flavoring credit of \$.34 = \$13.16 effective tax rate
 - \$.34 flavoring credit

Alcohol and Tobacco Tax and Trade Bureau



5010 Credit Computation (Cont'd)

**PG Spirits (\$13.50) + WG Wine Under 14% (\$1.07) +
WG Wine 14-21% (\$1.57) + PG Flavorings over 2.5% (\$13.50)**

**PG Spirits + PG Wines (All tax classes) +
PG Flavorings (Eligible and ineligible)**

Alcohol and Tobacco Tax and Trade Bureau



Batch

• Distilled Spirits	2,249.1 pg
• Eligible wine (14% ABV)	2,265.0 wg
• Eligible Wine (19% ABV)	1,020.0 wg
• Eligible Flavors	100.9 pg

Alcohol and Tobacco Tax and Trade Bureau



Determine 2.5% of Batch

- Distilled Spirits 2,249.1 pg
- Wine
 - 14% & Under: (2,265 * (.28)) 634.2 pg
 - 21% & Under: (1,020 * (.38)) 387.6 pg
- Flavors 100.9 pg
- Total 3,371.8 pg

$3,371.8 * (.025) = 84.3$ pg tax exempt flavors
 $100.9 - 84.3 = 16.6$ pg flavors that are taxed

Alcohol and Tobacco Tax and Trade Bureau



5010 Credit Computation (Cont'd)

Distilled Spirits	2,249.1 pg
Eligible wine (14% ABV)	2,265.0 wg
Eligible Wine (19% ABV)	1,020.0 wg
Eligible Flavors	100.9 pg

$$\frac{2,249.1(\$13.50) + 2,265.0(\$1.07) + 1,020(\$1.57) + 16.6(\$13.50)}{2,249.1 + 100.9 + (2,265 * (.28)) + (1,020 * (.38))} =$$

$$\frac{\$30,362.85 + \$2,423.55 + \$1,601.4 + \$224.10}{2,350.0 + 634.2 + 387.6} =$$

$$\frac{\$34,611.90}{3,371.8} =$$

\$10.27 effective tax rate

Alcohol and Tobacco Tax and Trade Bureau



How To Take 5010 Credit

- Credit can be taken by:
 - Effective tax rate per each batch of distilled spirits (27 CFR 19.35)
 - Standard effective tax rate for each product based on the least quantity and lowest alcohol content of the wine and/or alcohol flavoring ingredients that may be used in product (27 CFR 19.36)
 - Average effective tax rate which is based on the proof gallons in all batches of a product produced during the most recent six months (27 CFR 19.37)
 - Inventory reserve account which is based on establishment of an account for each product then proceeding on a first in, first out method (27 CFR 19.38)

Alcohol and Tobacco Tax and Trade Bureau

Effective Tax Rate:

26 USC 5010 and 27 CFR 19.34

Effective Tax Rate

- Attaches to cases to be paid based on 27 CFR 19.35
- Credit can be taken by:
 - Effective tax rate per each batch of distilled spirits (27 CFR 19.35)
 - Standard effective tax rate for each product based on the least quantity and lowest alcohol content of the wine and/or alcohol flavoring ingredients that may be used in product (27 CFR 19.36)
 - Average effective tax rate which is based on the proof gallons in all batches of a product produced during the most recent six months (27 CFR 19.37)
 - Inventory reserve account which is based on establishment of an account for each product then proceeding on a first in, first out method (27 CFR 19.38)

Alcohol and Tobacco Tax and Trade Bureau

5010 Credits

- Reduction of tax due per batch produced
- Based on flavorings (maximum \$.34 pg)
- Reduction taken on removal from bond
- Actual-Average-Standard
- Withdrawal FIFO or actual

Alcohol and Tobacco Tax and Trade Bureau

5010 Tax Credits: Imported Products

Karl Joedicke
Specialist,
Regulations and Rulings Division



Approval and Certification of Wine and Flavors Content 27 CFR 27.76

- a) Any person who...imports into the United States distilled spirits on which the tax is to be paid or determined at an effective tax rate based...on the alcohol content derived from eligible flavors...request and receive a statement of eligibility for each wine or flavor to be used in the computation of the effective tax rate.

Alcohol and Tobacco Tax and Trade Bureau



27 CFR 27.76 (Cont'd)

- b) To receive a statement of eligibility, the importer shall cause to be submitted to the TTB Alcohol and Tobacco Laboratory, 6000 Ammendale Road, Ammendale, MD 20705, the following:
- 1) An 8-ounce sample of each distilled spirits, wine, and flavor contained in the product; and

Alcohol and Tobacco Tax and Trade Bureau



27 CFR 27.76 (Cont'd)

- (2) A statement of composition for each ingredient
- (i) **For wine**, the kind (class and type) and percentage of alcohol by volume; and
 - (ii) **For flavors**, the name and percentage of alcohol by volume, and the name and quantity of each ingredient used in the manufacture of the flavor.

Alcohol and Tobacco Tax and Trade Bureau



27 CFR 27.76 (Cont'd)

- c) Each time distilled spirits containing eligible wine or eligible flavors are imported into the United States, the importer shall prepare a certificate of effective tax rate computation showing the following:
- 1) Name, address, and permit number of the importer;
 - 2) Kind (class and type) of product;

Alcohol and Tobacco Tax and Trade Bureau



27 CFR 27.76 (Cont'd)

- 3) Elements necessary to compute the effective tax rate in accordance with §27.40 are as follows:
- i. Proof gallons of distilled spirits (exclusive of distilled spirits derived from eligible flavors);
 - ii. Wine gallons of each eligible wine and the percentage of alcohol by volume of each; and
 - iii. Proof gallons on distilled spirits derived from eligible flavors.

Alcohol and Tobacco Tax and Trade Bureau

- 4) Date of the statement of eligibility of wines/flavors
- 5) Effective tax rate applied to the product
- 6) Signature

- d) Importer files certificate of Effective Tax Rate computation with Customs at the port of entry (if products imported in bottles). If imported in bulk, certificate furnished to proprietor of DSP to which the spirits are transferred.



Standard Effective Tax Rate 27 CFR 27.77

- a) In lieu of preparing a certificate of effective tax rate computation each time distilled spirits containing eligible wine or eligible flavors are imported as prescribed in §27.76(c), an importer may have a standard effective tax rate established based on the least quantity and lowest alcohol content of eligible wine or eligible flavors used in the manufacture of the product.

Alcohol and Tobacco Tax and Trade Bureau



27 CFR 27.77 (Cont'd)

- Summary of the remaining subsections (b) and (c):
 - Need the same flavor/wine samples and information as for the Statement of Eligibility;
 - Requires a sample of the finished product, and a statement of the composition of the finished product; and
 - Standard Effective Tax Rate for the product computed in accordance with §27.40(a) (Same as §19.34).

Alcohol and Tobacco Tax and Trade Bureau

SETR Approval Process

- Beverage Alcohol Laboratory evaluates samples and confirms declared use rate.
- Beverage Alcohol Laboratory sends results of analysis to the Regulations and Rulings Division.
- Regulations and Rulings Division confirms Standard Effective Tax Rate (SETR) requested and issues letter to importer approving or disapproving request.

Alcohol and Tobacco Tax and Trade Bureau

Turnaround Time

- Allow a two-month turnaround time from the time you submit samples to the Beverage Alcohol Laboratory to receipt of approval (or disapproval) from the Regulations and Rulings Division.

Alcohol and Tobacco Tax and Trade Bureau



Common Mistakes

- Incorrect calculation SETR
 - Must be computed in accordance with 27 CFR 27.40.
- Employing SETR prior to approval being granted
 - Importers must have authorization from TTB prior to employing SETR.

Alcohol and Tobacco Tax and Trade Bureau

5010 Tax Credit: Laboratory Analysis

Jeffrey Ammann, Ph.D.
**Chief, Beverage Alcohol
Laboratory**

- To analytically verify the use rate of an eligible flavor and/or eligible wine in a finished distilled spirits product to confirm the effective tax rate computation as described in 27 CFR 27.41, Computation of Effective Tax Rate.

- A flavor which:
 - Is eligible for drawback of tax under 26 U.S.C. 5134
 - Was not manufactured on the premises of a DSP
 - Was not subjected to distillation on a distilled spirits premises such that the flavor does not remain in the finished product



Eligibility Requirements (Cont'd)

- A wine which:
 - Does not contain more than 0.392 grams of carbon dioxide per 100 milliliters
 - Was not subjected to distillation at a DSP after receipt in bond
 - Must contain at least 20 ppm total fusel oil

Alcohol and Tobacco Tax and Trade Bureau



Sample Submission

- Include calculation of standard effective tax rate
- Send the finished product (750 mL) and at least 8 oz of eligible flavor, eligible wine, blenders, mergers, intermediates, and sugar syrups used in the production of the finished product to:

TTB - Beverage Alcohol Laboratory
National Laboratory Center
6000 Ammendale Rd
Beltsville, MD 20705

Alcohol and Tobacco Tax and Trade Bureau



Meaning of Terms 27 CFR 19.11

- **Proof:**
 - The ethyl alcohol content of a liquid at 60 °F, stated as twice the percent of the ethyl alcohol by volume
- **Proof Gallon:**
 - A gallon of liquid at 60 °F which contains 50 percent by volume of ethyl alcohol having a specific gravity of 0.7939 at 60 °F referred to water at 60 °F as unity, or the alcoholic equivalent thereof.
 - Also equal to wine gallon multiplied by proof/100

Alcohol and Tobacco Tax and Trade Bureau



Analyses Considerations

- Confirm if flavor has been evaluated by Nonbeverage Products Laboratory
- Analyze flavor for suitable target analyte
 - Use gas chromatography (GC), high pressure liquid chromatography (HPLC), or tandem mass spectrometry to determine the presence of an appropriate analyte common in both flavor and finished product
 - Propylene glycol
 - Vanillin
 - Quinine

Alcohol and Tobacco Tax and Trade Bureau



Analyses Considerations (Cont'd)

- Analyze flavor for suitable target analyte (cont'd):
 - Must analyze each component to ensure that only flavor and finished product contain analyte
 - Concentration of analyte is much greater in flavor, usually dilute in ethanol/water mixture
 - Certain analytes are not amenable for use rate determination
 - Analytes that may be found in every component
 - e.g., acetic acid, ethyl acetate, fusel oils
 - Determine the proof of the flavor, base, and finished product

Alcohol and Tobacco Tax and Trade Bureau



Use Rate Calculation

$$\frac{\text{Concentration of target analyte in finished product}}{\text{Concentration of target analyte in flavor}} \times \frac{\text{Proof of flavor}}{\text{Proof of finished product}} = \text{Use rate (\% on a proof gallon basis)}$$

Alcohol and Tobacco Tax and Trade Bureau



Lab Report to RRD

- Laboratory forwards laboratory analysis of each component in a submission to the Regulations and Rulings Division (RRD)
- Include a narrative for each component:
 - Identify the analyte selected to confirm use rate
 - For eligible wines, determine if contains > 20 ppm fusel oils
 - If the Laboratory determined that the use rate is within +/- 10% of claimed use rate, RRD will use proprietor's calculated effective tax rate
 - If the Laboratory determined that the use rate is more than +/- 10% of claimed use rate, RRD will use Laboratory's findings to calculate effective tax rate

Alcohol and Tobacco Tax and Trade Bureau



Lab Report to RRD (Cont'd)

- Laboratory will alert RRD if a component lacks a suitable target analyte and its addition can not be verified
 - If there is no reason to believe the flavor/wine was not added, then Laboratory will recommend to use proprietor's calculated tax rate

Alcohol and Tobacco Tax and Trade Bureau



Contact Information

- Dave Bateman, Distilled Spirits Industry Analyst
 - Dave.bateman@ttb.gov
 - 202-302-3859
- Karl Joedicke, Specialist
 - Karl.joedicke@ttb.gov
 - 202-927-8210
- Jeff Ammann, Chief, Beverage Alcohol Laboratory
 - Jeffrey.ammann@ttb.gov
 - 240-264-1596

Alcohol and Tobacco Tax and Trade Bureau