

2018

Position Paper

Wine & Spirits Business
Council (WSBC) the
European Chamber of
Commerce in Hong Kong



The contents of this publication are the sole responsibility of the European Chamber of Commerce in Hong Kong and reflect the Chamber's views only.

Spirits Tax Reform for A Competitive Spirits Showcase Market in the Region and Spirits Warehousing

1 Introduction

On behalf of the European Chamber of Commerce’s Wine & Spirits Business Council (WSBC¹), we wish to recommend that the Government review and pursue a more equitable spirits tax and regulatory environment for Hong Kong in order to remain competitive vis-à-vis its neighbours in the region. A reform of the current system will also enable Hong Kong to become a regional center for the premium spirits industry (including its related activities e.g. auctions), thereby reinvigorating the restaurant, bar and entertainment scene, and revitalizing Hong Kong’s tourism offer.

WSBC is also committed to reducing harmful drinking and advancing a balanced and inclusive regulatory and taxation environment that supports sustainable business growth, while cementing Hong Kong’s position as a leading business and travel destination. WSBC’s members strongly support the introduction of a Legal Purchasing Age in Hong Kong with the purpose of tackling underage drinking. We are also committed to playing a part in supporting the management and recycling of waste glass bottles in Hong Kong, through the Producers Responsibility Scheme on glass bottles, proposed at HK\$1/Litre bottle (subject to further implementation details). As regional competition intensifies, we look forward to contributing to and supporting a range of reforms that benefit Hong Kong citizens and the broader economy.

Issues and Recommendations for Policy Address

1. Spirits Tax Reform for A Competitive Spirits Showcase Market in the Region - To review the 24-year-old spirits tax system which taxes alcohol based on value; and to introduce a specific tax system based on alcohol content. WSBC is proposing a rate around HK\$75/Litre of pure alcohol (LPA), as a balanced approach for all stakeholders, for consideration.

2. Spirits Warehousing - To review and reassess the dangerous goods license requirement for the storage of potable spirits with more than 30% alcohol by volume (abv) in the Dangerous Goods Ordinance. The review should take into account the internationally accepted practices.

¹WSBC comprises six leading international wine and spirits companies including Edrington, Moët Hennessy Diageo, Pernod Ricard, Remy Cointreau, Teeling Whiskey, and William Grant and Sons. Together, these companies represent 45% of the “spirits market” in Hong Kong.

2 Spirits Tax Reform for A Competitive Showcase Market in the Region

Hong Kong bears one of the heaviest taxations on spirits (standards and above category) in Asia

Liquor with an alcoholic strength of more than 30% abv is the only dutiable commodity that is taxed based on its value, at 100% ad valorem since 1994. The reform of taxation on spirits (with >30% abv) is long overdue.

In 2004, the Government recognized in a public consultation exercise on alcoholic beverages tax, that “for high end products, [Hong Kong’s] duty is generally higher than major jurisdictions in the region and even some of the more mature European economies.” In the region, Hong Kong operators face one of the heaviest tax burdens on spirits, at 100% of import value, versus 33% in Mainland China, 40% in Macau, 39% in Taiwan, and 43% in Japan². In addition, ad valorem tax system is generally prone to under/mis-declaration by mala-fide operators, and thus requires stringent enforcement and constant monitoring.

We call for a simple, equitable and enabling spirits tax system - specific tax based on alcoholic content. This is consistent with international practice - many developed economies have already adopted a pure specific tax system on spirits e.g. the EU, the US, Australia, New Zealand, Japan, Malaysia, Singapore and Taiwan.

Reform to support a premium spirits center and secondary (auction) market

The abolishment of wine tax spurred Hong Kong to become Asia’s leading wine trade, distribution and auction center, successfully captured the booming wine consumption trend in China. The development of premium spirits industry, however, is restricted by the 100% spirits excise tax.

A reasonable specific tax rate will rationalize the tax burden on premium spirits, promote more choices of spirits, facilitate Hong Kong to become a regional showcase market, convert overseas purchases back to within Hong Kong, encourage visitors to purchase locally, attract new players and expand the footprint of related local organizations. The reform will be a catalyst and Hong Kong traders stand to gain competitiveness to create and offer a more diverse and vibrant portfolio of authentic premium spirits. This is particularly crucial in the borderless e-commerce marketplace.

² Comparison of total import and excise tax burdens on ad-valorem equivalence basis, using spirits with 40% abv, with retail value at around HK\$200/75cl bottle.

Today, the UK's secondary (auction) market of rare whiskies is the largest in the world, at the value of £25.06 million in 2017³. Hong Kong could also capitalize on the spirits tax reform and grasp the innovative business opportunity of rare whisky investment market in Asia. This could further grow the auction, brokerage and valuation businesses for investor grade whiskies, which is now sought after by connoisseurs, collectors and investors from all parts of the globe, including the burgeoning Asian middle class from Mainland China, India and South East Asia.

Revitalize tourism by invigorating a vibrant restaurant & bar scene

In comparison with the Greater Bay Area cities, Shanghai, Beijing, Macau, Taiwan, Singapore and Tokyo, F&B entrepreneurs and operators in Hong Kong are struggling to compete for a place in the World's 50 Best Bars due to the higher operational costs and limited spirits portfolio to create an innovative and unique entertainment and bar experience.

The proposed reform will energize the restaurant & bar scene with novel cocktails and premium offers. This will naturally revitalize tourism, and create a new landscape for other iconic events e.g. Whisky Live, Gin Jubilee, Cocktail Festival, etc. besides the annual Wine & Dine Festival and the biannual Vinexpo, and attract visitors from around the world.

Specific taxation: supporting public health objectives by targeting the harmful use of alcohol without impact on responsible drinking behaviour

A telephone survey⁴ to examine Hong Kong's citizens' current drinking behavior and the effects of the proposed spirits tax reform on citizens' drinking pattern was conducted by the Chinese University's Centre for Communication and Public Opinion Survey in August 2018. The survey interviewed 1,012 Hong Kong citizens aged 18 or above and found that 17.5% of interviewees had consumed spirits drinks⁵ in the past 12 months.

According to above-mentioned survey, 21.7% of alcoholic beverage consumers admitted being binge drinkers⁶ in the past 12 months. Taxing alcohol on the basis of its value does not address the negative externalities associated with alcohol consumption, whereas a specific tax system that taxes on the basis of its alcoholic content does. To help mitigate binge and excessive drinking, the proposed specific tax system on spirits would put a floor price on spirits, hence price of a product rises in line with its alcoholic content. Such a system is also endorsed by the WHO's Global Strategy to Reduce Harmful Use of Alcohol to "take into account, as appropriate, the alcoholic content of the beverage."⁷

In addition to binge drinking and harmful use of alcohol, the survey outcome indicates that the proposed spirits tax reform, which would replace the current ad valorem system with a spirits tax

³ Over £25M of Rare Whisky Sold at Auction, reported scotchwhisky.com, accessed at: <https://scotchwhisky.com/magazine/latest-news/17827/over-25m-of-rare-whisky-sold-at-auction/>

⁴ Conducted by interviewers using CATI (Computer Assisted Telephone Interview) system.

⁵ Include western spirits, Chinese spirits and spirits-based drinks (e.g. cocktail).

⁶ Binge drinking is a pattern of heavy drinking when consuming more than 60 grams of pure alcohol on a single occasion. In Hong Kong, 60 grams of pure alcohol is equivalent to approximately 5 cans of beers/ 5 glasses of table wine/ 5 pegs of spirits. One occasion refers to a period of few hours. Cited definition by Hong Kong Department of Health:

https://www.change4health.gov.hk/en/alcohol_aware/facts/binge_drinking/index.html

⁷ WHO, Global Strategy to Reduce Harmful Use of Alcohol, 2010a, p. 16

based on alcohol content set around \$75/LPA, would not have any quantitative impact on respondents' drinking pattern/habit one way or the other. Specifically, 81.5% of current spirits drinkers stated that they will not consume more spirits, whereas 97% of non-spirits drinkers⁸ indicated that they will not shift to spirits after the proposed tax reform. In addition, almost all abstainers (98.9%) will not start consuming spirits because of the tax changes.

Last but not least, WSBC fully supports the prohibition of sale and supply of intoxicating liquor to people under 18 years old pursuant to the Dutiable Commodities (Amendment) Ordinance 2018. To this end, the WSBC is ready to work with the government and other stakeholders to identify the best measures (including voluntary initiatives such as enhanced age verification and identification, point-of-sale messaging and retailers' staff training, etc.) to combat underage drinking in Hong Kong.

Recommendation

- (1) Review the 24-year-old spirits ad valorem tax regime;
- (2) Reform and introduce a specific tax system, based on the alcoholic strength of products. In particular, WSBC is proposing a rate around HK\$75/Litre of pure alcohol as a balanced approach for all stakeholders for consideration.

⁸ Alcoholic beverage drinkers who consume other alcoholic beverage except spirits.

3

Spirits Warehousing

In Hong Kong, a dangerous goods license is required for storage of potable spirits with more than 30% abv if the quantity is exceeding the stipulated levels⁹ pursuant to Clause 99 of the Dangerous Goods Ordinance (Cap. 295B). This is inconsistent with the international norms.

The dangerous goods license requirement does not only negatively impact on the efficient operations of the domestic markets; it also limits the number of bonded warehouse operators which could provide the spirits storage service for duty unpaid goods in large quantities. This undermines Hong Kong's competitiveness as a regional re-export hub for spirits when compared with other hub cities.

It is an internationally accepted practice that alcoholic beverages for human consumption are not subject to the dangerous goods regulations, hence the special storage license requirement. A list of the regulations in various countries is set out in the APPENDIX. WSBC recommends the Government to review and reassess the dangerous goods license requirement for the storage of potable spirits with more than 30% abv in the Dangerous Goods Ordinance. The review should take into account internationally accepted practices.

⁹ The stipulated levels: i) 12,500L in aggregate when packed in individual receptacles not exceeding a capacity of 5L and stored or used in premises protected throughout by automatic sprinkler installation; ii) 6,250L in aggregate when packed in individual receptacles not exceeding a capacity of 5L and stored or used in premises not protected throughout by automatic sprinkler installation; or iii) 2,500L in aggregate when packed in individual receptacles not exceeding a capacity of 5L and stored or used in any premises.

4 Conclusion

The Wine & Spirits Business Council and its members are looking forward to engaging with the Government, the Financial Services and Treasury Bureau, the Commerce and Economic Development Bureau, as well as other relevant government stakeholders to review and pursue a more equitable and enabling spirits tax and regulatory environment.

Appendix

Dangerous Goods Regulations in Various Countries

UN	<ul style="list-style-type: none"> Foods are usually out of the scope of the Globally Harmonized System of Classification and Labelling of Chemicals (GHS). In the <i>Model Regulations Recommendations on the Transport of Dangerous Goods</i>, alcoholic beverages with more than 24% but not more than 70% alcohol by volume, when carried in receptacles of 250 L or less, are not subject to the Regulations except for air transport.
EU	<ul style="list-style-type: none"> According to Article 1(5)(e) of Regulation (EC) No 1272/2008 the European Parliament and of the Council of 16 December 2008 on classification, labelling and packaging of (hazardous) substances and mixtures, the Regulation shall not apply to food or feeding stuff as defined in Regulation (EC) No 178/2002, which are in the finished state, intended for final user.
UK	<ul style="list-style-type: none"> The Planning (Hazardous Substances) Regulations 2015 make references to Regulation (EC) No 1272/2008 (above).
Australia	<ul style="list-style-type: none"> AS 1940 Standard for The Storage and Handling of Flammable and Combustible Liquids stipulates that it does not apply to the storage and handling of potable spirits having less than 24% v/v ethanol, and potable spirits with greater than 24% v/v ethanol in containers of less than 5 L capacity. AS 1940 defines “potable spirits” as liquids that are intended for human consumption, or are ingredients used in the production of such liquids, and which have a degree of strength not less than 24% alcohol (ethanol) by volume (v/v).
China	<ul style="list-style-type: none"> Regulation on the Safety Management of Hazardous Chemicals (2011 Revision) applies on “hazardous chemicals” regarding its production, storage, use, dealing and transportation. The Catalogue of Hazardous Chemicals includes only Denatured ethanol.
Singapore	<ul style="list-style-type: none"> According to Fire Safety Act, no person shall store or keep, or cause to be stored or kept, any class of petroleum or any flammable material except in or on licensed premises. The Complete List of Licensable Chemicals 2018 includes only Denatured ethanol. According to the information from Singapore Civil Defense Force’s website, food and beverages including beer, wine and liquor are exempted from P&FM license.
Taiwan	<ul style="list-style-type: none"> The Public Hazardous Substances & Flammable Pressurized Gases Establishment Standards & Safety Control Regulations establish standards governing location, construction and equipment of the places for manufacturing, storage or process of public hazardous materials and flammable pressurized gases; as well as safety control of their storage, process and handling. Flammable and combustible liquids include “Alcohols: a particle containing 1 to 3 Ca atoms and a saturated hydroxyl (including industrial alcohol) excluding the following materials: (1) Water solution with alcohol containment less than 60%; and (2) Flammable and combustible liquid containment below 60%, with flash point and combustion point both greater than those of water solution with alcohol containment not less than 60%.