BEER ASSOCIATION
OF SOUTH AFRICA

The Standing Committee on Finance
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RE: PUBLICATION OF THE 2021 DRAFT TAX BILLS FOR PUBLIC COMMENT

The Standing Committee on Finance call for public comment, relating to the 2021 Draft Rates and Monetary Amounts and Amendment of Revenue Laws Bill ('Rates Bill') refers.

Introduction

The Beer Association of South Africa ('BASA') represents the beer industry in South Africa. Its membership includes The Craft Brewers Association of South Africa (CBASA), Heineken South Africa, and South African Breweries.

The beer industry is a key contributor to the South African economy. In 2018 the beer industry contributed 1.53% of GDP. The GDP multiplier is 1.4 which is the same as the mining industry. From 2015 to 2018 the beer production industry generated a total GDP impact of R387.1 billion. Between 2015 and 2018 the brewing industry supported between 146 898 and 210 136 jobs and in 2018 supported 1.4% of national employment. In 2018/19 government raised an estimated R25.1 billion from excise tax on alcohol products, which is about 1.9% of total tax haul. It is estimated that the outlets in townships provide a form of income to between 180 000 and 265 000 people. Beer manufacturers also provide several social and economic upliftment programs across the country with an emphasis on supporting entrepreneurs and small business development.

BASA was mandated by its members to make representation to the Standing Committee on Finance ('SCoF') in relation to the Rates Bill, such representation to be submitted on 30 August 2021. In addition, such supplemented representation has been made to the National Treasury ('Treasury') and the South African Revenue Service ('SARS') for which submission was required by 28 August 2021.

Background

It is with great appreciation that BASA engages the prestigious bodies in relation to the draft Rates Bill as it forges a strong relationship between the economic recovery of South Africa, the tax incidence, and the impact of the tax incidence on business and ultimately the consumer.

The former Honourable Minister of Finance Mr. Tito Mboweni ('The Minister of Finance') tabled the Rates Bill on 24 February 2021 ('2021 Budget Speech'). This Rates Bill provided for an increase of 8 percent in Excise Duties for all liquor categories. Details to these adjustments are set out in Part 2A of Schedule No. 1 to the Customs and Excise Act 91 of 1964 ('the Act').

In this submission, BASA, wishes to comment on the 8 percent increase in Excise Duties as announced in the 2021 Budget Speech.

The 8% increase as expressed in the 2021 Budget Speech has three challenging factors that BASA believe should be considered by Treasury:

1. The increase is nearly double the Inflation Rate.
2. The increase is in contradiction to Government's current Excise policy framework.
3. The impact of the Excise Duty increases on the Beer Value Chain from Barley to Bar.

It is disappointing that despite several requests to engage with Treasury on the above concerns prior to the announcement of the increase being made, Treasury maintains its position; as tabled by The Minister of Finance in the 2021 Budget Speech announcing an Excise Duty increase of 8%. This represents an increase at almost double the rate of inflation (4.2%), and therefore double the rate expected in terms of the current excise policy framework. In particular, our submission will comment on the intentional deviation of the 2021 excise rate from the Alcohol Tax Policy Principles and Guidelines of 2014 and its impact on the beer industry and the value chain we support. This deviation between the policy framework and its implementation has a compounding effect not only ultimately to the consumer but moreover contributing to a negative investor sentiment.

The negative investor sentiment emanates from an inability to rely on a transparent fiscal policy to plan which is further exacerbated by a volatile economy and the protracted effects of the Covid-19 pandemic('pandemic').

South Africa, as the rest of the world, has experienced the ebbs and flows of a volatile economy. This scenario facing South Africa and the associated challenges have in recent times been further exacerbated by the impact of the pandemic. This pandemic continues to have a severe impact on multiple levels both international and specifically in South Africa. It is undeniable that the impact from an economic perspective has been most severe on industries directly impacted by the restrictions imposed in the varying National Government instituted Lockdown Levels. The alcohol industry has been one of the most severely impacted by these restrictions imposed during Lockdowns; in that the local sale of alcohol related products were prohibited.

This prohibition saw a loss to the GDP of R64,8 billion which is equal to 1.3 % of the GDP. A decline in Sales Value of R45.1 billion. A potential job loss of 1,59% of formal and informal sector employment with 248, 759 jobs.

BASA on behalf of its members wishes to engage Government, with these comments to the Rates Bill based on the following arguments:

1. The intention of Excise Duties and whether this will be achieved by an increase of 8%
2. Reflection on tax incidence over the past five years and why the 8% increase will have a further adverse impact

3. The impact of the 8% Excise Duty increases on the already strained Beer Value Chain
4. The unintended consequence of the 8% Excise Duty increases
5. Proposal from BASA that will assist in ensuring the survival and recovery of the beer value chain

1. Excise Duties

Excise duties and levies are imposed mostly on high-volume daily consumable products (e.g., petroleum and alcohol and tobacco products) as well as certain non-essential or luxury items (e.g., electronic equipment and cosmetics). The primary function of these duties and levies is to ensure a constant stream of revenue for the State, with a secondary function of discouraging consumption of certain harmful products; that is, harmful to human health or to the environment ("Excise | South African Revenue Service", 2021).

From the extract, Excise Duties have two core functions.

1. A constant revenue stream for the State.
2. Discouraging consumption of harmful products.

Tax incidence has far outgrown the economic viability relative to the Inflation Rate. The Excise Tax instrument, therefore, can no longer be a viable economic growth or stimulus metric without due consideration for the related tax incidence.

The secondary function, from the beer industry's perspective should be further refined into two key areas.

1. Discouraging consumption.
2. Harmful products.

The former argument has been postulated on several occasions and numerous studies thereto have been published. The argument could fairly be made from either perspective; whether for or against; whether increasing Excise Duties has the intended consequence as set out or whether such increase has unintended consequences. It is indeed the position of BASA that the unintended consequence of Excise Duty increases far outweighs the value proposition of discouraging consumption, let alone of “harmful products”.

It is with the latter argument to the secondary function that the beer industry wishes to draw distinction between itself as an alcoholic beverage with a low ABV of 2,8 to 6 % alcohol and other alcoholic beverages with high ABV’s of 40%.

Beer is a fermented beverage with a low concentration of pure alcohol relative to other products. Beer is 90% water: it is bulky, heavy, perishable, and fragile, needing protection from light, heat, and oxygen.

Brewing is primarily a local business. Most main brewing inputs like barley, hops and yeast are sourced locally or in neighbouring countries. The beer industry has demonstrated a meaningful intent in recent years to reducing the alcohol content of its products with its no and low alcohol beers. While this reduction in alcohol content is a demonstration of intent it is unfortunate that the South African consumers are slow to gravitate to this offering.

It should be noted that in the proffered arguments related to “harmful products” that the beer industry does not wish to cast a shadow on other alcoholic products. The beer industry wishes to express, unequivocally, that independent studies clearly drawing this distinction does exist. In addition, the beer industry in South Africa has in recent years made concerted efforts to educate the consumer to the harmful effects of alcohol abuse and the indirect effects excessive consumption of alcohol has to society at large.

BASA does submit however, that products with the low ABV like beer, should not be viewed through the same lens as other alcoholic products with higher ABV, and the proposed tax rate should not be increased by the same relative percentage as that to other alcoholic products.

It is common practice to regulate alcoholic beverages based on beverage type and strength. Many OECD countries tax spirits higher than beer, in terms of excise per liter of pure alcohol In addition, many use progressive excise taxation within beer, encouraging production and consumption of even lower alcohol strength products. Namely, Australia, Canada, Denmark, Finland, France, Iceland, Ireland, Israel, Mexico, Netherlands, New Zealand, Norway, Portugal, Spain, Sweden, Switzerland, and the UK.

In light of the argument presented; in relation to the harmful nature of alcoholic products, but differentiation with respect to beer; the position by Government expressed by the Minister of Finance in the 2021 Budget Speech that the increase in Excise Duty of 8% on alcohol products as a result of the harm associated with these products should not be blanketly adopted in relation to the beer industry. It is therefore advocated that a revised reduced increase at inflation or below should be applied to it.

2. Tax Incidence

While Excise Duties is undeniably deployed as a viable instrument by Government as a constant revenue stream; and the requirement thereto given the economic impacts in recent years cannot be ignored; the element of tax incidence cannot be detached from the relative economy.

According to the current excise policy, the adjustment in Excise Duties is calculated based on the tax burden derived from projected prices for the next fiscal year or the expected Inflation Rate, whichever is higher. However, as will be demonstrated and is acknowledged by Government this position and the adoption thereof is disparate to say the least.

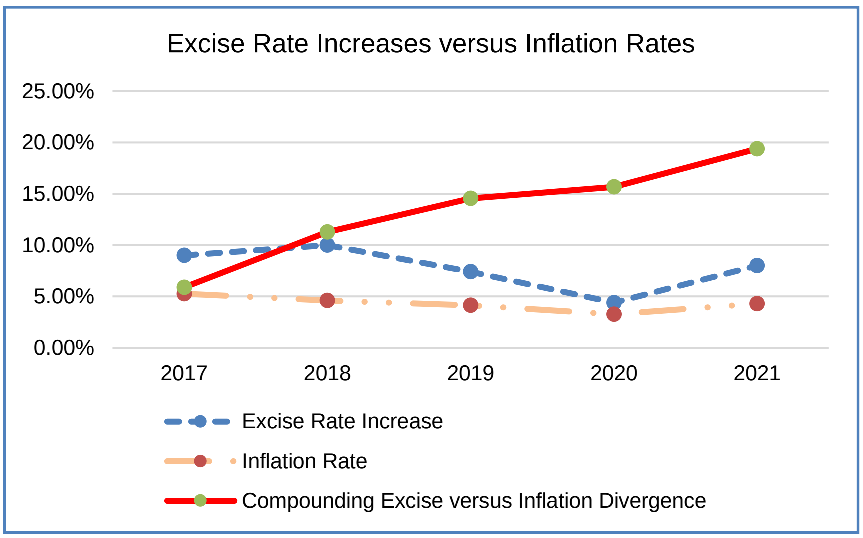
The increases in Excise Duties, with specific reference to Tariff Item 104.10.20 (Beer Other) in Part 2A of Schedule No. 1 to the Act, over the past five years have been higher than the inflation rate. This relative divergence from the inflation rate over the past five years has undeniably had a compounding relative economic effect.

As expressed by the illustration of historic Excise Duty Rates relative to the Inflation Rate below:

	2017	2018	2019	2020	2021
Excise Duty Rate	86.39	95.03	102.07	106.56	115.08
Excise Rate Increase	9.00%	10.00%	7.41%	4.40%	8.00%
Inflation Rate	5.27%	4.62%	4.13%	3.27%	4.28%
Excise Rate versus Inflation Rate Variance	3.73%	5.38%	3.28%	1.13%	3.72%

("Inflation rate: South Africa | Statista", 2021)

This demonstrated divergence from the Inflation Rate of the relative year-on-year increases in Excise Duties has resulted in a cumulative variance of 17,23% over the past five years as can be observed below:



From the depiction it is clear that the relative year-on-year increases in Excise Duty rates over the past five years has incrementally widened the gap between the Excise Duty rate and the relative annual Inflation Rate. Ultimately, as will be elaborated upon in “Tax Increase on Beer Value Chain Impact”, in relation to the Tax Incidence ultimately the burden of above inflation increases is not on the producers but ultimately on the consumers based on the elasticity of the industry. Which has a further unintended consequence dealt with in this submission of consumers moving to the illicit industry should the product become unaffordable.

The illustration above is well recognised by Government in that it acknowledges that “Excise Duties have been increasing above inflation in most recent years” (2021). However, despite this recognition Government continues the move of the Excise Duties incidence further above its own policy guidelines (2014). The increases in Excise Duty rates above the policy guidelines by Government not only has a negative effect on the tax incidence but also egregiously impacts on investor sentiment as it does not portrait a government with stable fiscal policy.

Further, with many of the larger beer players being multinationals with global boards to report to. It is difficult to justify investment in South African operations with the continuous above inflationary increases as they will rather then look at other countries to invest in where the excise policy is more consistent and in line with the countries performance. We saw this during the lockdown with both SAB and Heineken halting their investments worth millions of Rands in South Africa. A Heineken plant in KZN that was meant to provide over 400 jobs did not go ahead. Similarly, SAB opened up operations in Mozambique; these operations could possibly have come to South Africa creating employment. With our unemployment rate at its highest, these are serious considerations that need to be borne in mind.

While this argument has previously been proffered by industry; given the current economic climate; the journey to recovery will only suffer if an increase in Excise Duty is considered beyond that of the Inflation Rate. While convergence between the historic trends is unlikely, an 8% increase in Excise Duty would further compound the historic divergence from the Inflation Rate. At minimum, given the factors under consideration, an increase in Excise Duties should be considered in line or below the Inflation Rate.

3. Tax Increase of 8% and impact on Value Chain from Barley to Bar and ultimately on the Consumer

When Excise Duties are applied the consideration is narrowly viewed as having an impact on the specific manufacturer in the industry, however, as would be argued; the impact of Excise Duties (in effect the Tax Incidence) reverberates throughout the value chain from the farmer who grows the hops and barley, the suppliers to the industry being packaging companies, equipment providers and technicians, transport industry, advertising agencies, to the bar, retailers and restaurant who sells the product and ultimately partial pass through to the consumer, who is sensitive to price changes in beer beverages.

Unlike Value Added Tax (VAT), which is recoverable by the VAT vendor throughout the value chain, Excise Duties, while a consumption tax originates at the start of production.

Tax legislation applicable to Excise Duties in beer are administered on a Duty at Source (DAS) basis. The Excise Duties incurred during manufacturing and removal is levied by the manufacturer but subsequently passed on throughout the supply chain. While this is an efficient mechanism for tax administration; the unintended consequence of DAS in the beer industry is that the Excise Duty levied at production is ultimately levied at a multiplier effect on the consumer.

Given a typical supply chain and a meagre mark up of 15% throughout the supply chain; the Excise Duty to the consumer would relatively be around R 231,47 per litre absolute alcohol *(around R 10 per average litre beer) as opposed to the R 115,08 per litre absolute alcohol *(around R 5 per average litre beer) which, in this element, contributes to the fiscus as the actual Excise Duty.

From the illustration, the impact of the increases in Excise Duties, as a consumption tax, is absorbed by the consumer at a rate double that of the Excise Duty levied.

Given this, it is contended that due consideration should be given to the consumer when considering Excise Duty increases, especially given the current economic climate and that another above Inflation Rate increase of 8% would have throughout the supply chain and ultimately the consumer.

The real concern however is that the consumer who finds the legal product too expensive will move to the cheaper illicit products, which are both harmful to the consumer as well as to the fiscus. With the alcohol industry and its value chain as a collective having contributed close to R200 bn in GDP in 2019, R72 billion in indirect taxes and supporting millions of livelihoods.

4. Unintended consequences of 8 %Tax Increase

It is an unfortunate reality in South Africa that consumers of alcohol are not subject to instinctive behavioural change, i.e., that the consumers behaviour would change because of external factors such as rate increases. Over the past period of the pandemic several reports have demonstrated that the average consumer would find means to secure a supply of alcohol. This "Comment" in relation to Excise Duty increases is not offered up as a platform to debate the impact of the potential alcohol abuse in South Africa; but rather to express those external factors have no impact on the relationship of the South African consumer with alcohol.

Evidence has shown as demonstrated by several independent research and publications; that indeed the opposite as to what was intended during the pandemic was achieved in that consumers sought out forms of illicit alcohol ("Booze ban fuelled increase in illicit alcohol, with spirits in high demand: report", 2021).

There are several extracts, arguments and independent research demonstrating the unintended consequence of alcohol prohibition; some of which are supported by the very findings and interactions by SARS. No more telling is the impact of the illicit alcohol market than expressed by the Commissioner of SARS during several media briefings ("Tackling illicit alcohol trade in South Africa 'critical' to economic recovery - The Drinks Business", 2021), support the very argument that the unintended consequence of excessive taxation is the probable growth in an Illicit Economy.

This assertion is further supported by the findings of a recent Euromonitor Report that the sale of illicit alcohol products in South Africa now accounts for 22% of the alcohol market in South Africa by volume and 12% by value (2020). This equates to R20.5bn. The losses to the fiscus accounts for a staggering R11.3bn which has seen a growth of 20% (CAGR) since the report was last commissioned in 2017.

Legal alcohol is in competition with illicit alcohol as a result of the increasing in Excise Duty rates faster than inflation. This is further compounded in the beer industry as beer prices grow slower than inflation in light of the challenging consumer environment. This makes beer sales less profitable, damaging the competitive prospects for beer, as taxed alcohol, relative to the illicit alcohol available in the market.

It is undeniable then as expressed above that consumer behaviour in South Africa is unlikely to change because of external forces, let alone an increase in Excise Duties. On the contrary, the consumer is more likely to seek out “tax free” alternatives, as is expressed and well documented. This is the space wherein the Illicit Alcohol Economy is proven to thrive.

Given the unintentional consequence of Excise Duty increases, it is advocated that at most an increase relative to that which the consumer can tolerate within the extent of the Inflation Rate or below, should be considered as a means to counteract the unintentional growth in the Illicit Alcohol Economy.

5. Proposal to ensure survival and recovery of Beer Value Chain

In addition to that referred to in *“1 – Excise Duties”* relating to the less harmful nature of alcoholic products with a low ABV like beer compared to other alcoholic products; the beer industry also prides itself on the basis of entrepreneurship. The beer industry finds itself in a space representing both large corporates as well as entrepreneurs.

Entrepreneurial beer manufacturers (Craft Brewers) are an integral facet to the industry Craft Brewers are supported by the large corporates such as Heineken South Africa and South African Breweries since their product offering is not in direct competition. Entrepreneurship and the related Small, Medium and Micro Enterprises (SMME); is vital for the economic recovery of South Africa.

The entire industry suffered great losses during the pandemic and related periods of alcohol sale prohibition. An 8% increase, the pandemic as well as bans have succeeded in killing the craft sector. The Craft Beer sector though suffered such losses to the extent that many such entrepreneurs in this sector had to cease operations (Mashego, 2021). Sadly, the industry has been offered little to no relief, except for a deferral which for a small craft brewer on the brink of closure offers very little relief. Brewers were advised that they do not qualify for UIF TERS as well as other relief mechanisms that were offered to other industries including the announcement by the President providing a relaxation on licences except for liquor licences.

Sadly, within the current tax legislation, SMMEs in beer manufacturing, are not sufficiently recognised or provided relative relief in relation to Excise Duties to incubate growth in this sector. Furthermore, large corporates are not incentivised to support such SMMEs in their development. It is the position that not only should Craft Brewers be given a degree of relief; but that in addition, large corporates should be incentivised by degrees of tax relief in their demonstration of developing this vital contributor to the South African economy.

The position presented by Government in its "Economic Reconstruction and Recovery Plan" is to stimulate equitable and inclusive growth (2021). With reference to the differentiation in the Beer Industry, an 8% increase in Excise Duty is not complimentary to the intent by Government. Such an increase above the Inflation Rate will only further disadvantage this vital contributor to South Africa's path to economic recovery.

These craft brewers in particular need urgent relief to prevent extinction and an 8 % increase will not be that relief that they so desperately need.

Conclusion

As set out in this Comments presented by BASA, on behalf of its members, we humbly request that National Treasury should give careful and due consideration to the elements of:

1. The intention of Excise Duties in relation to alcoholic strength and the harmful nature differentiates Beer from other Alcoholic Beverages.
2. Reflection on tax incidence over the past five years and its compounding impact has shown a cumulative deviation of 17,23%. This is a strong deviation from the Governments Tax Policy.
3. The impact of Excise Duty increases on the Value Chain which is ultimately absorbed by the Consumer.

4. The unintended consequence of Excise Duty increases which stimulates the growth in the Illicit Alcohol Economy.
5. The Beer industry also incorporates the Craft Beer Entrepreneurs who have suffered greatly during the Covid-19 pandemic. Like other SMMEs, they are pivotal for the Economic Recovery of South Africa and cannot afford the impact of an 8% increase in Excise Duty.

It is without question that yet another increase in the Excise Duty rate on beer above the Inflation Rate is neither beneficial to government nor to industry; let alone the compounding effect on the consumer. In addition, the deviation by Government from its own fiscal policy is counterproductive to economic recovery as it decimates investor confidence.

As an industry we wish to appeal to Government to consider the factors and arguments presented in this submission with the view of stabilising the economy by maintaining and operating within the existing policy framework.

It is with these due considerations, as articulated herein, that the Beer Industry advocates for the disjuncture between the excise policy framework and its implementation to be minimised. In particular, an 8% increase in excise and any other above inflation increases in excise, have a negative economic impact on the beer industry and its viability. the maintenance in the current Excise Duty rate; a below inflationary increase or at minimum an increase which is commensurate to the Inflation Rate.

We would appreciate an opportunity to make presentations at the portfolio committee hearings commencing on the 31 August 2021 to provide further clarity on our submission above.

Yours Sincerely,

Patricia Pillay
CEO of Beer Association of South Africa

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