Institute of Alcohol Studies

BRIEFING

Budget 2017 analysis

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Summary

- Alcohol duty was cut in real terms for the fifth year out of six
- A new duty rate for ciders between 6.9% and 7.5% was announced, to come into effect in February 2019
- This is intended to incentivise strong cider producers to reformulate their products – if it works, a three-litre bottle of white cider will contain 20.4 rather than 22.5 units
- Accounting for inflation, beer duty is now 16% lower than in 2012; cider and spirits duty 8% lower, and wine duty 2% lower
- Cumulatively, these policies will cost the Treasury over £1 billion in 2018/19, and a total of £8.1 billion in the ten years to 2023
- Lower duty causes death and illness – the 2015 Budget was estimated to cause 6,500 more hospitalisations each year due to alcohol
- The evidence that duty cuts benefitted pubs is sketchy, as brewers have retained the savings and off-licenses have continued to undercut them

Overview

This document summarises the decisions taken on alcohol duty in November's Budget, and evaluates their likely impact. It also sets these policies in the context of recent history, and takes stock following another real terms cuts to duty, the fifth since 2012: cheaper alcohol, lower Treasury revenues, higher consumption, increased illness and death, and no demonstrable benefits for pubs.

What happened to alcohol duty in the Autumn Budget?

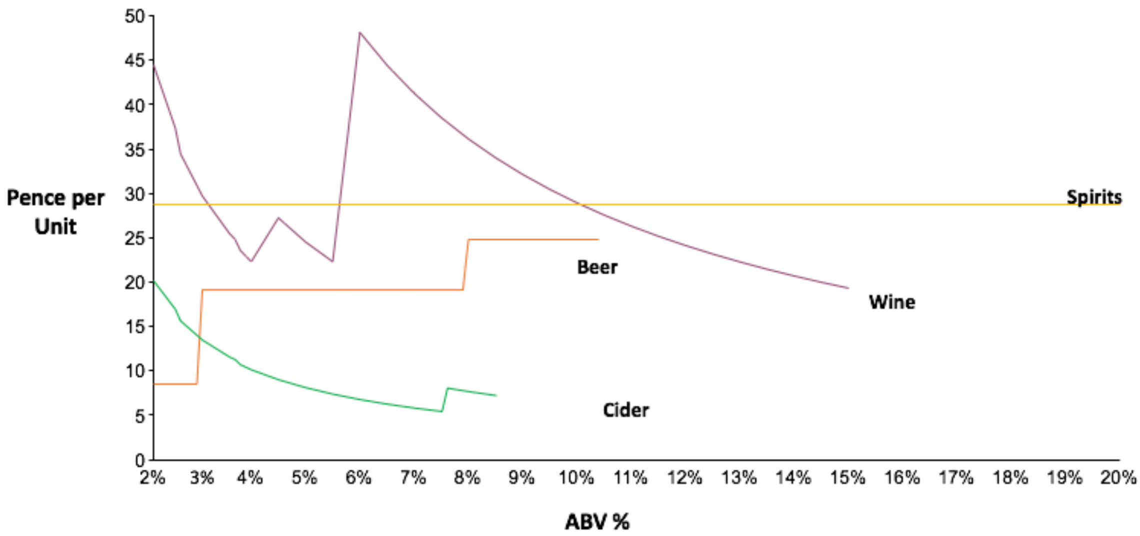
In the Autumn Budget, delivered on 22nd November, the Chancellor announced the following policies:

- A freeze on duty on all alcohol for 12 months from February 2018 (a real terms cut, since duty will fail to keep pace with inflation)
- A new band of duty on ciders between 6.9% and 7.5% ABV to come into force from February 2019 (though the specific rate has not been set)

A modest tweak to cider tax

In the Spring Budget of March 2017, following a long campaign led by the Alcohol Health Alliance, the Government announced that it was consulting on a new rate of cider duty to target high strength 'white' ciders, such as Frosty Jack's and White Ace. These products have been particularly associated with harmful, street and dependent drinking. They are typically 7.5% ABV, since this is the point attracting the lowest duty per unit of any alcoholic product, as figure 1 illustrates.

Figure 1: Duty per unit by alcohol type[1]



The Institute of Alcohol Studies had called for this new rate of duty to be levied on all ciders between 5.5% and 7.5% ABV, to produce a meaningful increase in the price of strong cider.[2] By contrast, the **Government's favoured approach** is to use the new duty band to **incentivise white cider producers to reformulate their product** to a lower strength.[3] However, the effectiveness of this measure seems to be restricted by the Government's determination to minimise the impact on mainstream cider producers. This appears to be the reason behind setting the lower bound of the new rate at 6.9% ABV: the Government estimates that 11.5% of the cider market is between 6.9% and 7.5% ABV, of which 78% is white cider.[4] The net result of such a high lower bound is that if white ciders are in fact reformulated to avoid it, this will only have a small effect on their strength. To illustrate, a three-litre bottle of 6.8% ABV cider would contain **20.4 units of alcohol, compared to the 22.5 units** in the 7.5% ABV products on sale today. The effective duty per unit, as figure 2 shows, would rise from 5.4p to 5.9p. By contrast, a beer of 7.5% ABV is taxed at 19.1p per unit, and a 5.0% ABV cider is taxed at 8.1p per unit.

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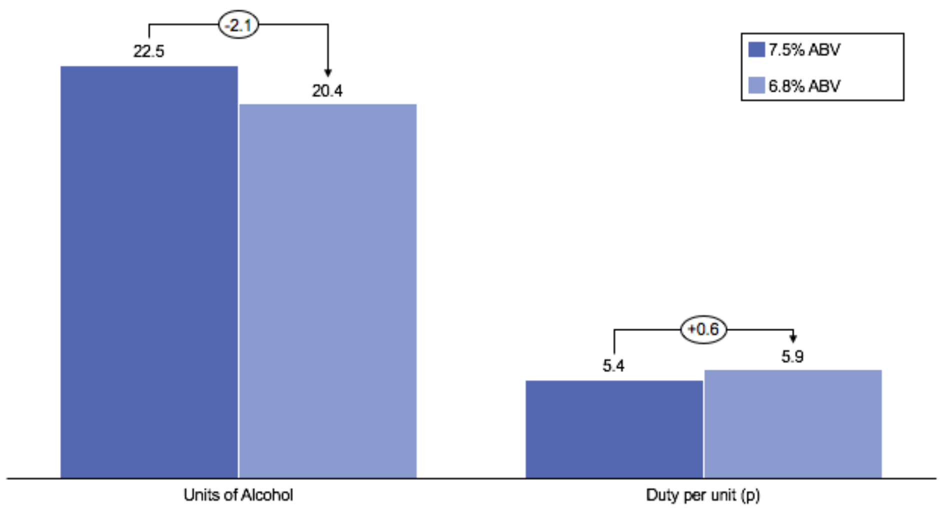
[1] HM Revenue & Customs (2017), Alcohol Duty rates from 13 March 2017. Available from: <https://www.gov.uk/government/publications/rates-and-allowance-excise-duty-alcohol-duty/alcohol-duty-rates-from-24-march-2014>
[2] Institute of Alcohol Studies (2017), IAS response to HM Treasury Alcohol structures consultation. Available from: <http://www.ias.org.uk/uploads/pdf/IAS%20consultation%20responses/cr57062017.pdf>
[3] HM Treasury (2017), Autumn Budget 2017, p. 38
[4] HM Treasury (2017), Autumn Budget 2017 Duty on high strength ciders. Available from: <https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/661438/duty_on_high_strength_ciders.pdf>

Figure 2: Impact of Reformulation from 7.5% ABV to 6.8% ABV for three-litre bottle of cider priced £3.59



In order to give cider producers time to reformulate their product, the introduction of the new duty rate will be delayed until February 2019. This means that almost **two years will have elapsed** between the Government first signalling its intention to address white cider in the March 2017 Budget and it actually taking action. This delay further undermines the policy because the Government has chosen to freeze alcohol duty in the interim. This means that **tax on strong ciders will fall** in real terms before the new rate is introduced.

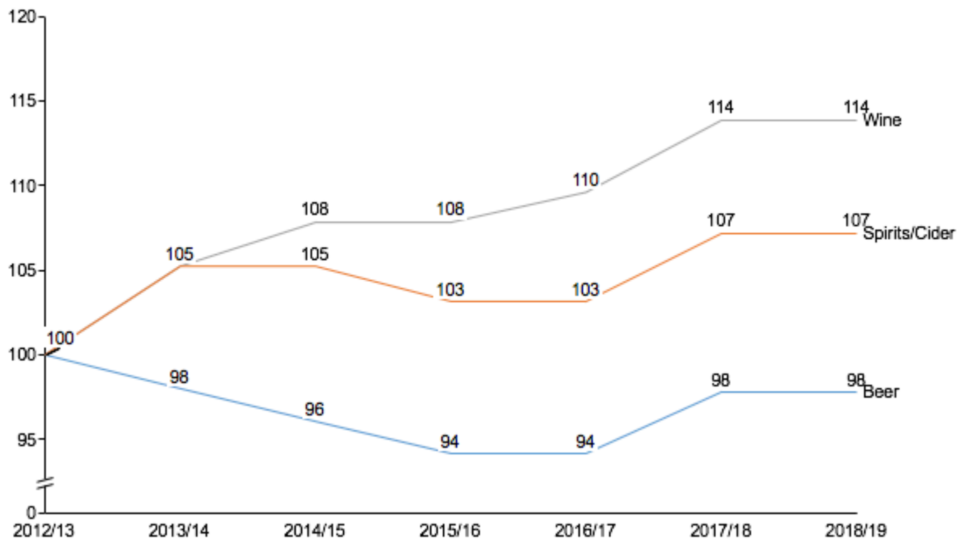
The Government is yet to confirm what the new rate of tax will be on ciders between 6.9% and 7.5% ABV. However, since it has not proposed any change to the rate on ciders above 7.5%, the new rate will almost certainly be lower than the >7.5% rate – otherwise, there would be a perverse incentive to produce stronger cider. This implies that the new duty rate at most be £61.04 per hectolitre or 8.0p per unit.

Another real terms reduction in alcohol taxes

For the fifth year out of six, the Government cut alcohol duty in real terms. Between 2008 and 2012, the alcohol duty escalator automatically increased alcohol duties by 2% above inflation each year. However, this was scrapped for beer in 2013 and for wine, cider and spirits in 2014. Alcohol duties were cut or frozen in 2015 and 2016. They were all increased in line with inflation in the 2017 Spring Budget in March, but the last week's Autumn Budget revealed that they will be frozen for a year from February 2018.

The charts below show the cumulative impact of these measures. In nominal terms, successive duty cuts have reduced beer duty by 2% since 2012; cider and spirits are 7% higher; and wine duties are 14% higher.

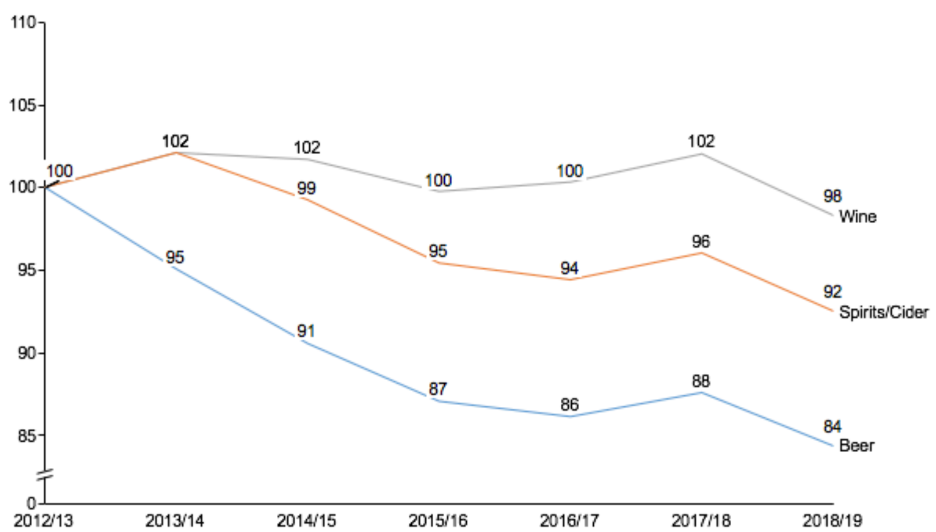
Figure 3: Nominal Duty Rates, Indexed: 2012/13=100[5]



However, this picture looks dramatically different if we account for inflation, which has eroded much of the value of duty since 2012. Moreover, with the Office for Budget Responsibility forecasting inflation of 3.1% in 2018/19, the freeze announced in the most recent Budget will have a particularly negative effect on duty rates. As a result, in real terms by 2018/19, compared to 2012:

- **Beer duty will be 16% lower**
- **Cider and spirits duty will be 8% lower**
- **Wine duty will be 2% lower**

Figure 4: Real Duty Rates, Indexed: 2012/13=100[6]



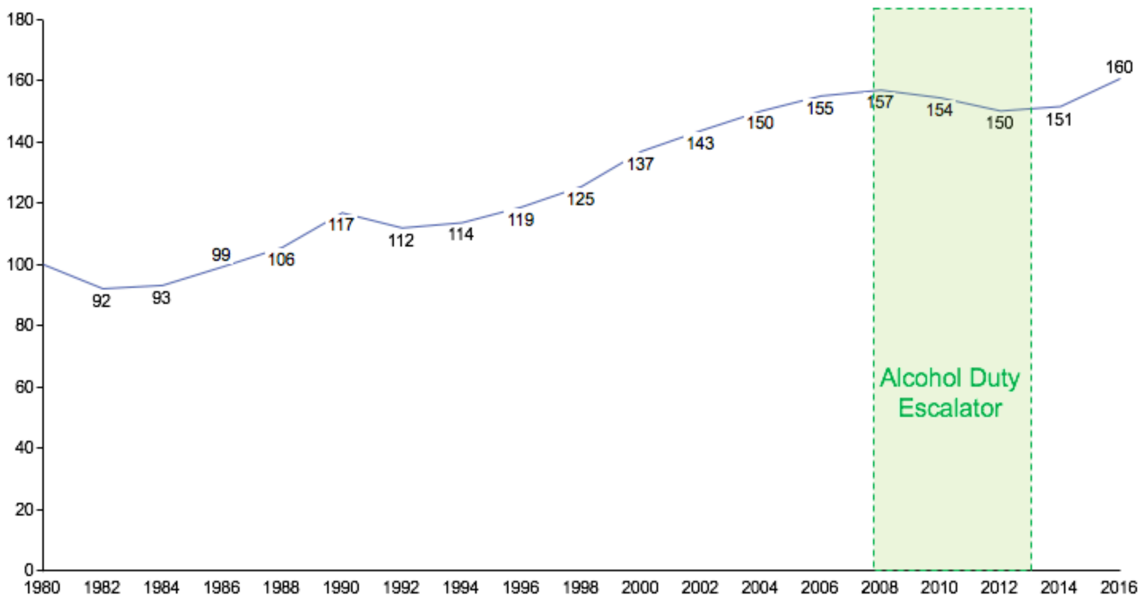
[5] General beer duty; still 1.2-7.5% ABV cider and perry; 5.5-15% ABV wine. Source: HM Revenue & Customs (2017), Alcohol Duty rates from 13 March 2017; HM Revenue & Customs, Alcohol Bulletin
[6] General beer duty; still 1.2-7.5% ABV cider and perry; 5.5-15% ABV wine. Source: HM Revenue & Customs (2017), Alcohol Duty rates from 13 March 2017; HM Revenue & Customs, Alcohol Bulletin; OBR, Economy Supplementary Tables November 2017

The Government also announced a shift in the scheduling of changes to alcohol duty. In recent years, the convention had developed that the government would only amend alcohol duty rates in the Spring Budget in March, and these changes would come into force immediately. However, with the Government moving to a single Budget each year, alterations to alcohol duties will from now on be announced in the Autumn Budget in November, and only come into force in February. One concern regarding this shift is that alcohol producers may be able to minimise their duty liability by releasing greater quantities of their product for tax clearance early in anticipation of a duty rise or holding it back in anticipation of a duty cut.

What is the impact on prices and affordability?

These reductions in alcohol duty have contributed to lower prices and the growing affordability of alcohol, and as such endanger public health. Affordability is widely recognised as one of the key drivers of consumption and harm, with cheaper alcohol invariably leading to higher rates of death and disease.[7] Having declined slightly in the period of the duty escalator, affordability has begun to climb again since its repeal, as figure 5 shows. As of 2016, alcohol was 60% more affordable than in 1980.

Figure 5: Alcohol Affordability Index, 1980-2015 (Indexed, 1980=100)[8]



What is the impact on the government finances?

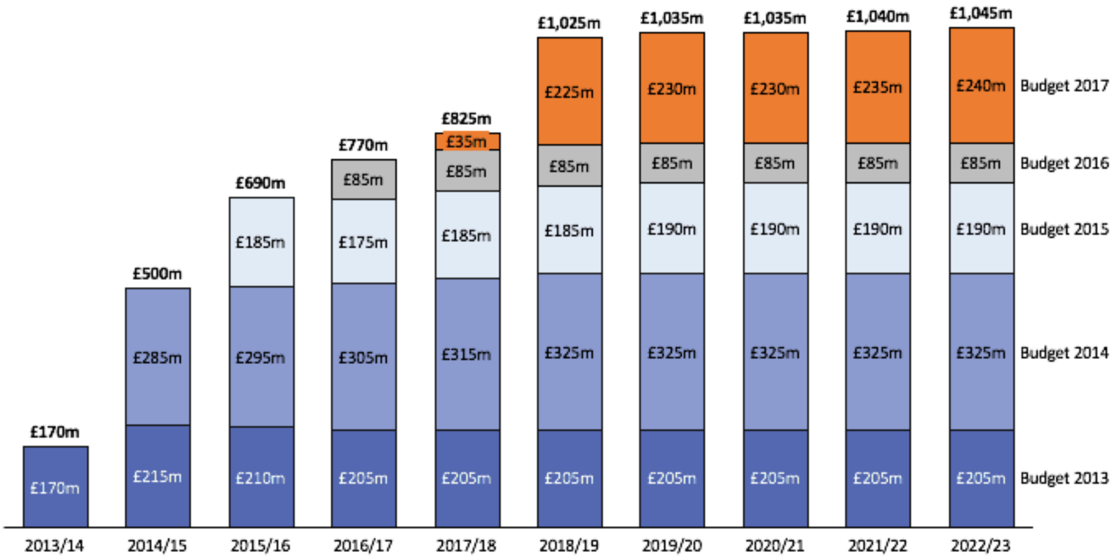
The Treasury estimates that the freeze on alcohol duties in the 2017 Autumn Budget will cost the Exchequer £35 million in 2017/18, then £225 million in 2018/19 and over £230 million every year thereafter: in total over £1.2 billion over the next six years.

This merely compounds the lost revenue of the past six Budgets. Extrapolating from the Government's official estimates, we calculate that from 2019, **cuts to alcohol duty will be**

[7] Wall, M & Casswell S (2013), Affordability of alcohol as a key driver of alcohol demand in New Zealand: a co-integration analysis, *Addiction* 108:1, pp. 72–9
[8] NHS Digital (2017), Statistics on Alcohol, England, 2017

costing over £1 billion each year. By 2023, the **cumulative cost over ten years is set to hit £8.1 billion**.

Figure 6: Annual Loss of Alcohol Duty Revenue Due to Budget Decisions[9]



What is the impact on health?

We do not have the capabilities to specifically model the health impacts of the Government's changes to alcohol duty. However, it is highly likely that as the affordability of alcohol has increased, consumption will rise, with a negative impact on health. University of Sheffield analysis has estimated that **an additional 6,500 people will be hospitalised every year with alcohol-related ailments as a result of the 2015 Budget alone**.[10] We can therefore infer that the total negative impact of removing the duty escalator and subsequent cuts to duty is higher still, with tens of thousands suffering. It is notable that alcohol-related deaths in England have started to rise since the duty escalator was abolished.[11]

What is the impact on pubs?

Cuts to alcohol duty are often justified on the basis that they benefit pubs. Yet duty cuts also help supermarkets and off-licenses reduce their prices and undercut pubs. Last year, a number of pub owners wrote to the Chancellor to bemoan the failure of duty cuts to benefit their businesses: "the brewers impose increases every January onto the retailers and then ask the government to reduce duty in March – at the fiscal expense of other tax raising – in order to mitigate the outcry and demand effect".[12] They conclude that the actions of the brewers undermine the effects of a duty cut to such an extent that "they are not saving a single pub with their actions".[13] Such suspicions are somewhat borne out by academic

[9] HM Treasury (2013), Budget 2013; HM Treasury (2014), Budget 2014; HM Treasury (2015), Budget 2015; HM Treasury (2016), Budget 2016; HM Treasury (2017), Autumn Budget 2017
[10] School of Health and Related Research, University of Sheffield (2015) The Sheffield Alcohol Policy Model [Poster]. Research impact and Parliament, 2 November, Portcullis House, Houses of Parliament, London
[11] ONS (2017), Statistical Bulletin: Alcohol Related Deaths in the United Kingdom: Registered in 2015
[12] Sutherland, E. (2016), Leading operators slam 'flawed' BBPA beer duty campaign, *Publican's Morning Advertiser* [online]. Available: <http://www.morningadvertiser.co.uk/Legal/Legislation/Leading-operators-slam-flawed-BBPA-beer-duty-campaign>
[13] Ibid

evidence that prices for cheap alcohol, as in supermarkets, are more sensitive to changes in tax than more expensive products such as those found in pubs.[14]

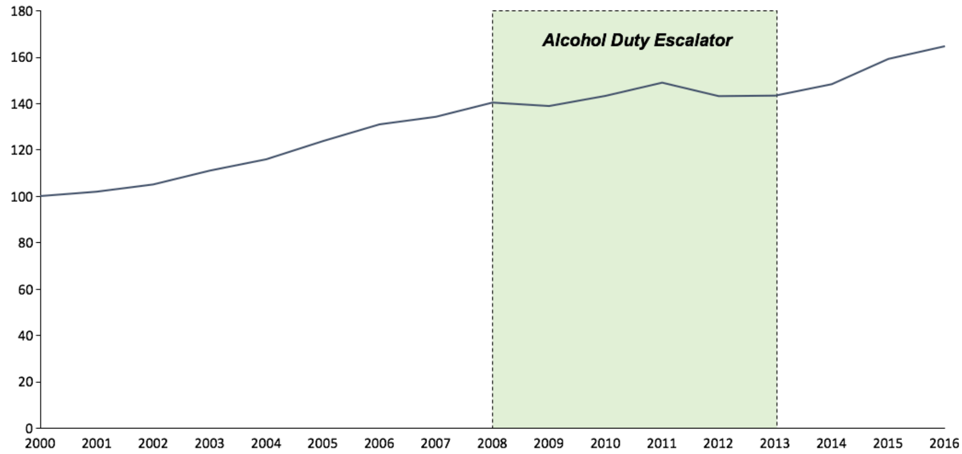
The shift from on-trade to off-trade is largely a function of the growing price differential between the two. Yet in the lifetime of the duty escalator, the premium on beer in the on-trade grew at a slower rate than either before or after. In the duty escalator period, higher beer taxes ensured that prices in the off-trade rose almost as quickly as prices in the on-trade: 4.0% per year, compared to 4.5%. In the time either side of the duty escalator, prices fell in the off-trade, but continued to rise in the on-trade.

Figure 7: Annual Beer Price Growth in the on-trade and off-trade[15]

	Q1 2000 – Q1 2008	Q1 2008 – Q1 2012	Q1 2012 – Q1 2017
On-trade	3.5%	4.5%	2.3%
Off-trade	-1.1%	4.0%	-0.7%

The chart below shows the effect of these changes on the price differential between the on and off-trade, which grew rapidly between 2000 and 2008, slowed while the duty escalator was in force, and has been rising again since 2013.

Figure 8: Ratio of On-trade and Off-trade Beer Duty Retail Price Indices (Indexed, Q1 2000=100)[16]



Thus it is unclear that cutting duty has helped pubs, rather than continuing the shift from on-trade to off-trade.

[14] Ally, A.K. et al (2014), Alcohol tax pass-through across the product and price range: do retailers treat cheap alcohol differently? *Addiction* 109:12, pp. 1,994–2,002
[15] ONS, Time Series: RPI: alcohol drink. Available from: <http://www.ons.gov.uk/economy/inflationandpriceindices/timeseries/dobj/mm23>
[16] Ibid

IAS recommendations

1. **Meaningfully increase the price of high strength cider.** The introduction of a new rate of duty on high strength ciders is a promising step in the right direction. However, the band is too narrow to produce a significant increase in the per unit price of white cider. We recommend a wider rate of duty, starting from 5.5% ABV, and steps towards bringing tax on cider into line with beer.

2. **Reinstate the duty escalator.** Alcohol is 60% more affordable today than it was in 1980. The duty escalator temporarily reversed this trend by raising alcohol taxes above inflation, with predictable benefits to public health. We know that affordability drives consumption, so increases in duty are necessary to address the growing issue of cheap alcohol, and the worrying signs that progress on alcohol harm is stalling.

3. **Implement a minimum unit price for all alcoholic products.** MUP is needed to deal with the particular problem of the cheapest strongest drinks favoured by the heaviest drinkers and is complementary to reforming the alcohol duty structure for other products. Following the recent Supreme Court ruling that the policy is compliant with EU law, the Scottish Government is set to implement MUP from May 2018. The governments of Wales, Northern Ireland and the Republic of Ireland have also signalled their intentions to introduce it, and the Westminster Government should not be left behind.

4. **In forthcoming trade agreements, ensure the government can protect public health through measures like scaled volumetric taxation**. As the Government renegotiates the UK's trading relationship with the European Union and the other countries, it should ensure that trade regulations do not excessively constrain its ability to protect public health. In particular, it should seek no longer to be bound by European directives in a way that means it is not possible to tax wine or cider in proportion to their alcohol content, so that it can introduce scaled volumetric taxation and ensure stronger drinks are always more expensive.

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Our core aim is to serve the public interest on public policy issues linked to alcohol. We do this by advocating for the use of scientific evidence in policy-making to reduce alcohol-related harm.

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