



Ho Chi Minh City

Response Paper

January 24, 2014

Follow-Up Comments Relating to
AmCham's Jan. 14 Meeting with Ministry of Finance
Concerning Proposed Excise Tax on Carbonated beverages

Introduction

Vietnam is currently considering a proposal to levy an excise tax on *nước ngọt có ga không cồn* (literally translated “non-alcohol sweetened beverages with gas,” i.e., carbonated soft drinks). Sweetened beverages without gas (such as sweet tea or fruit-flavored beverages) would be exempt from this tax.

AmCham is very concerned about the proposed excise tax on carbonated beverages. American carbonated beverage brands have long been, and continue to be, the global leaders in the carbonated beverage market,¹ and several of AmCham's members produce carbonated beverages. As the proposed excise tax will affect our members' businesses, AmCham has engaged the Vietnamese government to learn more about the tax. To date, however, AmCham has not received any evidence or policy rationales that would support levying a tax on beverages based on CO₂ content.

AmCham had a productive meeting with the Ministry of Finance (“MOF”) on January 14, 2014, during which AmCham expressed its concerns about the proposed excise tax's expected impact on its members. The MOF indicated that the matter was still open. At the close of the meeting, the MOF requested further information concerning the effects of CO₂ consumption on human health, the dynamics and breakdown of the carbonated beverage market, and whether the

¹ U.S.-based brands account for a large portion of the global carbonated beverage market because carbonated beverages are a historically American product. Practically all of the recipes for the major carbonated beverages on the market today trace back to 19th-century American pharmacies, where they were developed to mask the taste of bitter medicinal extracts and powders that were used at that time. American pharmacists discovered that the effervescence effect of CO₂, when combined with sugary syrups, served to distract the taste buds from the bitter taste of the drugs. Coca-Cola, Pepsi, citrus-flavored phosphate soda (the precursor to 7up and Sprite), Dr. Pepper, ginger ale, root beer, and sarsaparilla soda (known as *sáxì* in Vietnam) were all invented by American pharmacists in the 19th-century. U.S.-based companies still use these century-old recipes used to make their beverages, giving American companies a cultural and competitive advantage over companies located in countries that do not have a tradition of pharmacies developing carbonated beverages to make medicines.

proposed excise tax conforms to international norms. The response paper will provide the additional information that the MOF requested.

1. Health Effects of Carbonated Beverage Consumption

The assertion that carbonated beverages contribute to obesity, stomach problems, and ulcers has no support in medical literature. We evaluate each of these claims below.

a. Obesity

The claim that beverage carbonation, by itself, contributes to obesity has no basis in respected medical scholarship. In fact, research suggests that carbonation may actually be beneficial in combating obesity, as carbonated beverages are associated with greater feelings of satiety and significantly lower food intake.

A study published in the *British Journal of Nutrition* demonstrated that increasing the level of carbonation in a beverage increases satiety and decreases later intake of calories.² Researchers found that, “[c]ompared with the beverage with low carbonation, consumption of the beverages with medium and high carbonation led to significantly higher satiety until lunch, when intakes of food and energy were significantly lower.”³ In other words, individuals who drink carbonated beverages before meals feel fuller and eat less, which could lead to lower levels of obesity. These results were replicated in other studies, which also demonstrated that individuals feel satiated quicker and thus end up consuming a lesser amount when drinking carbonated beverages than when drinking noncarbonated beverages.⁴

b. Digestive issues

The argument that carbonated beverages are harmful because they interact with stomach acid to “create pressure on the stomach and intestines”⁵ is also an unsubstantiated claim. Research published in the *Journal of Food Science* found that carbonated beverages do not cause damage to the gastrointestinal tract.⁶ Other recent studies even suggest that carbonated beverages are actually beneficial for digestive and cardiovascular health. Carbonated water has been used for centuries to treat digestive complaints, and a study published in the *European Journal of*

² S.A. Moorhead et al., *The level of carbonation of a sugar-sweetened beverage preload affects satiety and short-term energy and food intakes*, 99 BRIT. J. NUTRITION 1362 (2008).

³ *Id.* (emphasis added).

⁴ GP Lambert et al., *Effects of carbonated and noncarbonated beverages at specific intervals during treadmill running in the heat*, 2 INT’L J. SPORT NUTRITION 177 (1993); Dennis H. Passe et al., *The Effects of Beverage Carbonation on Sensory Responses and Voluntary Fluid Intake Following Exercise*, 7 INT’L J. SPORTS NUTRITION 286 (1997).

⁵ *Do you think the country should impose a tax on soft drinks?* VIỆT NAM NEWS, July 12, 2013, <http://vietnamnews.vn/opinion/your-say/241998/do-you-think-the-country-should-impose-a-tax-on-soft-drinks.html>.

⁶ R.E. Kleinman, *Protection of the gastrointestinal tract epithelium against damage from low pH beverages*, 73 J. FOOD SCI. 99 (2008).

Gastroenterology and Hepatology confirmed that carbonation relieves indigestion and constipation symptoms.⁷

c. Stomach ulcers

The link between carbonated beverages and stomach ulcers is an outdated myth. It used to be thought that carbonated beverages contributed to the development of ulcers. In recent years, however, Nobel Prize-winning research by Dr. Barry Marshall demonstrated that the bacterium *Helicobacter pylori* (*H. pylori*), not diet, is the cause of stomach ulcers.⁸

2. The Carbonated Beverage Market

Carbonated beverages account for only 28% of total Non-Alcoholic-Ready-To-Drink (“NARTD”) beverages sold in Vietnam.⁹ Of this small portion of the overall NARTD market, foreign manufacturers’ products account for 88% of carbonated beverages sold in Vietnam,¹⁰ similar to the foreign share in other nearby markets.¹¹

The share of the overall beverage market that would be affected by the excise tax is small. Carbonated beverages are not as popular in Vietnam as they are in other countries, accounting for only about a quarter of the overall NARTD market. This is in addition to a worldwide trend in which “carbonated beverage consumption has been on the decline since the late ‘90s as consumers have turned to newer, non-carbonated beverages such as bottled waters, coffees, teas, sports and energy drinks.”¹² Furthermore, if an excise tax is placed on carbonated beverages, producers will be forced to pass this cost on to consumers, driving demand down even more. Combined, these factors indicate that an excise tax carbonated beverages will not raise significant tax revenues, and revenue could very well be lower than forecasted due to decreasing demand.

In addition, market share statistics show that the proposed excise tax will fall almost exclusively on foreign brands, giving the excise tax a clear appearance of protectionism. The Vietnamese media has already portrayed the tax in protectionist terms; when the excise tax on carbonated

⁷ R. Cuomo et al., *Effects of carbonated water on functional dyspepsia and constipation*, 14 EUR. J. GASTROENTEROLOGY & HEPATOLOGY 991 (2002).

⁸ See, e.g., C. Holden, *Triumph of the Ulcer-Bug Theory*, 310 SCIENCE 34 (2005). P. M Hellström, *This year’s Nobel Prize to gastroenterology: Robin Warren and Barry Marshall awarded for their discovery of Helicobacter pylori as pathogen in the gastrointestinal tract*, 12 WORLD J. GASTROENTEROLOGY 3126 (2006); Francis Mégraud, *A Humble Bacterium Sweeps This Year’s Nobel Prize*, 123 CELL 975 (2005).

⁹ Calculation based on data reported by Nielsen through its Retail Index Service for NARTD categories in 2013, in the markets as defined by The Nielsen Company. (Copyright © 2014, The Nielsen Company.)

¹⁰ *Id.*

¹¹ Pitsinee Jitpleecheep, *Coke gassed as Pepsi fizzles*, BANGKOK POST, March 5, 2013, available at <http://www.bangkokpost.com/learning/learning-from-news/338932/soft-drinks-coke-rises-pepsi-falls>

¹² Karlene Lukovitz, *Fitch: Big Beverage Company Growth Lies Overseas by Wednesday*, MARKETING DAILY, July 23, 2008, available at <http://www.mediapost.com/publications/article/87061/fitch-big-beverage-company-growth-lies-overseas.html?print>

beverages was proposed, the Vietnamese media highlighted the fact that the tax would give Vietnamese non-carbonated beverage brands a price advantage over predominately-foreign carbonated beverage brands.¹³

Due to the media attention, foreign companies and investors are already very sensitive to the possible protectionist effects of the carbonated beverage tax. The appearance of protectionism in such a high-profile market will almost certainly raise the issue of fairness, and undermine investor confidence. If enacted, the excise tax will invite high-profile challenges under Vietnam's free trade treaties and agreements. In light of the Vietnamese government's resolution in early 2014 make a renewed effort to attract greater foreign direct investment in Vietnam, this excise tax could undermine Vietnam's overall FDI strategy.

3. International Practices and Trends

Our research has uncovered no other existing excise tax similar to the one that Vietnam is considering. All other nations that levy an excise tax on non-alcoholic beverages do so broadly; no nation levies an excise tax exclusively on carbonated beverages. Vietnam's proposed excise tax is the only one of its kind.

The MOF cited Thailand, Cambodia, and India as countries that it understood to have similar taxes. These countries, however, have broad-based excise taxes on many types of NARTDs. Cambodia, for example, levies a tax of "10 percent on all types of beverages."¹⁴ Other nations do not single out carbonated beverages for taxation, as the excise tax under consideration would do.

Broad-based taxes on beverages in other countries are the only point of comparison Vietnam has for reference, and it should be noted that these types of taxes reflect a fairly new and unproven policy, and are also highly unpopular and controversial. Consumers do not appreciate novel taxes, and many proposals for beverage taxes have been quickly rescinded after sparking public

¹³ *Do you think the country should impose a tax on soft drinks?* VIỆT NAM NEWS, July 12, 2013, <http://vietnamnews.vn/opinion/your-say/241998/do-you-think-the-country-should-impose-a-tax-on-soft-drinks.html> (stating that Vietnamese beverage companies "focus on non-carbonated drink products, leaving the carbonated drinks to the production of foreign giants"). The media has repeatedly pointed out that foreign brands have an advantage in the carbonated beverage market; see Bich Diep, *Beverage industry thrives despite tough times*, DTINews.VN, 15 Aug. 2013, <http://www.dtinews.vn/en/news/018/30577/beverage-industry-thrives-despite-tough-times.html> (quoting VBA statement that "[o]nly a few Vietnamese beverage companies" can compete with well-known foreign branded beverages); *Weak management sends Tribeco packing: experts*, THANH NIEN NEWS, 17 Aug. 2012, <http://www.thanhniennews.com/2010/pages/20120817-tribeco-disband-losing-competition-weak-managing.aspx> (indicating that Vietnamese companies have largely conceded the carbonated beverage market to the internationally-recognizable brands, because "[i]n the tough race with other major beverage groups in the world, Vietnamese brands can only exist when they develop products in 'different branches' to avoid direct competition" with global brands).

¹⁴ KINGDOM OF CAMBODIA MINISTRY OF ECONOMY AND FINANCE TAX DEPARTMENT, LAW ON TAXATION CHAPTER 4, § 1, ARTICLE 85 (*emphasis added*).

backlash. Experts have criticized such taxes as arbitrary, ineffective, and regressive.¹⁵ As a result, the movement to tax beverages has lost momentum in recent years.

Numerous jurisdictions that have experimented with such taxes have later repealed them. For example, countries including Argentina, Denmark, the Dominican Republic, Egypt, Ghana, Indonesia, Pakistan, the Philippines, South Africa and Zambia (among others), along with several U.S. states, either have reduced or eliminated taxes on beverages.

4. Other Considerations

In addition to the information requested by MOF at the January 14 meeting, we would also like to address some comments made at the meeting concerning the general basis of excise taxes.

First of all, at the meeting, the MOF noted that Vietnam has excise taxes on non-luxury products such as motor vehicles, tobacco, and alcoholic beverages, and that this suggests that revenue alone is enough to justify levying an excise tax on any product. According to Oxford Economics and the International Tax & Investment Center, however, “food and non-alcoholic beverages have fundamentally different attributes compared to normally excisable products, such as motor vehicles and parts, beverage alcohol, [and] tobacco, and are not usually subject to excise tax for these reasons.” For example, “according to the seminal IMF Tax Policy Handbook, [the] best practice is to limit discriminatory taxes (typically implemented via excise taxes) to products that cause negative externalities or are luxury goods, or where such taxes result in a more progressive tax base and/or deliver efficient revenue generation.”¹⁶

The non-luxury items mentioned by the MOF that are subject to an excise tax—motor vehicles, tobacco, and alcoholic beverages—carry significant external costs for the state. The users of motor vehicles, for example, travel on roads that cost the government an enormous amount to construct and maintain. Tobacco products cause health problems that prove costly for the government and society (such as increased health care costs, loss of tax revenue from impaired taxpayers, increased social security and welfare costs when families lose a breadwinner to lung cancer, etc.). Alcohol products carry external costs borne by the government (such as increased spending on law and order to control intoxicated citizens, losses associated with alcohol-related motor vehicle accidents, loss of tax revenue caused by decreased taxpayer productivity, etc.). Carbonated beverages simply do not carry the kinds of external costs that justify levying excise taxes on alcohol, tobacco, and motor vehicle products.

As for the other criteria laid out by the IMF, none of them apply to carbonated beverages. Regarding luxury product taxation, carbonated beverages are not a luxury good. Carbonated beverages are widely consumed by individuals at every income level, and are in the same price-range as non-carbonated beverages.

¹⁵ See, e.g., OXFORD ECONOMICS AND INTERNATIONAL TAX & INVESTMENT CENTER, THE IMPACTS OF SELECTIVE FOOD AND NON-ALCOHOLIC BEVERAGES TAXES 2 (2013).

¹⁶ *Id.*

As to creating a progressive tax base, a tax on carbonated beverages would undermine this objective, as it would be a regressive tax. “[T]he poorest consumers spend a greater proportion of their income on food and non-alcoholic beverages than wealthier households,”¹⁷ so a tax on carbonated beverages would place a greater burden on low-income consumers than wealthy consumers.

Finally, a tax on carbonated beverages would not deliver efficient revenue generation. As already discussed in Section 2 (The Carbonated Beverage Market), market factors indicate that an excise tax on carbonated beverages will not raise significant tax revenues, and revenue could be lower than expected due to decreasing demand caused by the tax itself. As the Oxford/ITIC notes, “[i]f the goal of [a selective food and non-alcoholic beverages tax (SFBT)] is to produce tax revenue, an SFBT should generally be applied to products that are price inelastic,”¹⁸ meaning that a price increase associated by an excise tax will not proportionately lower demand. However, “[i]n developing countries, consumption of some items, such as carbonated soft drinks, is extremely price elastic. In these cases, imposing a tax may lead to significantly lower demand for that particular product and may therefore not generate additional tax revenue for governments.”¹⁹

The proposed tax on carbonated beverages fails all four of the IMF’s criteria for an excise tax. The IMF tests demonstrate that the carbonated beverage tax is an unusual and highly arbitrary tax policy.

In addition to the IMF criteria, the Oxford/ITIC lists some other considerations and drawbacks that governments should take into account when considering new excise taxes:

- New excise taxes have the potential to reduce other forms of tax revenue (e.g. corporate income tax and employment-related taxes) that are paid by producers, wholesalers and retailers of the taxed products, their associated suppliers, and their employees.
- New excise taxes can lead to increased trans-border purchasing to avoid the tax increase, as consumers choose to purchase from a location where the tax is lower. While this may sound far-fetched, the main reason Denmark repealed its beverage tax was because Danes began crossing the German border in huge numbers to do their grocery shopping after the tax was imposed.²⁰
- New excise taxes will impose increased administrative costs on the government to cover the design, monitoring, and enforcement of the tax.

¹⁷ *Id.*

¹⁸ *Id.*

¹⁹ *Id.*

²⁰ *Denmark gives into pressure from cross-border German competition: Repeals soda tax*, BEFORE IT’S NEWS, April 29, 2013, <http://beforeitsnews.com/libertarian/2013/04/denmark-gives-into-pressure-from-cross-border-german-competition-repeals-soda-tax-2500924.html>; *Denmark Hopes Cheaper Soda Will Boost Economy*, DER SPIEGEL, April 23, 2013, available at <http://www.spiegel.de/international/europe/denmark-to-repeal-tax-on-soda-and-beer-to-limit-cross-border-shopping-a-895857.html>.

- Excise taxes increase costs to business as companies are forced to spend more time meeting their regulatory obligations imposed by the tax. To avoid the administration and reporting burden imposed by SFBTs and the impact of the tax on profits, companies may even relocate operations to countries where operating costs are lower.

RECOMMENDATION

AmCham sees no reason to impose an excise tax on carbonated beverages, and many reasons not to impose such a tax. The excise tax will not improve the physical health of Vietnamese citizens. It will disproportionately burden foreign-branded products, giving the strong appearance of protectionism. There is a possibility that the tax could be found by international trade bodies to violate Vietnam's free trade agreements, and it will certainly erode foreign investors' confidence in Vietnam's commitment to the national treatment principle. No other nation singles out carbonated beverages for taxation. Excise taxes on beverages are unpopular with the public and with public policy experts. Several jurisdictions have been forced to abandon their broad-based beverage tax in recent years. There are no externalities associated with CO₂ in beverages. Carbonated beverages are not a luxury item. An excise tax on carbonated beverages is a regressive tax. An excise tax on carbonated beverages is not an efficient or significant source of new tax revenue.

In light of these facts, we do not understand why the MOF has chosen carbonation as the basis for an excise tax. There appears to be no logical basis for targeting carbonated beverages for taxation.

We would like to meet with the MOF again, at the Ministry's convenience, for further discussion. Specifically, we would like to discuss the policy rationale for singling out CO₂-content as the basis for beverage taxation. When we meet, we will provide scholarly reference materials for the Ministry's consideration.