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FINANCIAL SERVICES AND THE
TREASURY BUREAU

Central Government Offices,
Ice House Street,
Hong Kong

Urgent by Fax (2509-9055)

27 May 2009

Ms Joanne MAK
Clerk to Bills Committee
Legislative Council Secretariat
Legislative Council Building
8 Jackson Road
Central
Hong Kong

Dear Ms MAK,

**Bills Committee on Dutiable Commodities (Amendment) Bill 2009 (the Bill)
Follow-up Actions from Meeting held on 21 May 2009**

Further to the Bills Committee meeting held on 21 May 2009, I set out below our response to the follow-up actions raised by Members.

The Effectiveness of Combating Illicit Cigarettes

2. The Hong Kong Customs and Excise Department (C&ED) has been taking robust enforcement actions against illicit cigarette activities. Since the levying of the new tobacco duty as announced in the Budget, C&ED has been closely monitoring illicit cigarette activities at the entry points and on the street level, and has strengthened its enforcement actions against different aspects of illicit cigarette activities, including smuggling, storage, distribution and peddling. Tactically, with enhanced intelligence collection, C&ED will not only crack down on the smuggling sources, but will also conduct intensive operations against retailing and peddling of illicit cigarettes. C&ED will also spare no effort to monitor and combat the sale of illicit cigarettes through phone order leaflets.

3. As a result of its enhanced enforcement effort, C&ED detected 955 cases involving smuggling, storage, distribution or peddling of illicit cigarettes in the first four months this year. The number of seizure cases has increased as compared with the same period in the past two years but there has not been significant change in the quantity of illicit cigarettes involved (see table below). According to C&ED's intelligence analysis and observation, there is no sign that illicit cigarettes activities have become more rampant.

	2007 (Jan-Apr)	2007	2008 (Jan-Apr)	2008	2009 (Jan-Apr)
No. of cases (smuggling, distribution, storage & peddling of illicit cigarettes)	638	1,819	461	1,601	955
No. of arrest	481	1,446	350	1,207	715
Quantity of cigarettes seized (million sticks)	26	109	22.5	73	25
Value of seizures (HK\$ million)	38	160	34	110	44
Duty Potential of seizure (HK\$ million)	21	87	18	59	26

Increase of Tobacco Duty Rates and Drug Abuse

4. According to C&ED's intelligence, there has been no significant change in the price of common illicit drugs from January to April 2009. As the latest figure on the number of drug abusers is only available up to the end of 2008, we at this stage do not have any data to assess the impact of tobacco duty rates increase on the number of drug abusers.

Sales of Duty-Free and Duty-Paid Cigarettes and the Impact of Tobacco Duty Rates Increase on Tobacco Retailers

5. The monthly average sales of duty-free cigarettes (sold by duty free shops in Hong Kong control points and those in Luohu, Huanggang, Macau and Futian) for the two months preceding the tobacco duty increase (i.e. January and February) was 157,570 thousand sticks. After the increase of tobacco duty rates on

25 February 2009, the average monthly sales for March and April 2009 was 155,620 thousand sticks, which was similar to that for the period right before the duty increase and that (154,750 thousand sticks) for the same period last year. The duty potential of the duty-free cigarettes sold in March and April 2009 was \$375 million.

6. C&ED do not collect retail statistics of cigarettes. The table below shows the changes in duty-paid quantity of cigarettes in the first four months of 2008 and 2009 –

	2008		2009	
	Duty-paid Quantity (in 10,000 sticks)	Decrease (%)	Duty-paid Quantity (in 10,000 sticks)	Decrease (%)
Jan & Feb (monthly average)	56,045	-	46,274	-
Mar & Apr (monthly average)	6,893	88	10,614	77

The figures show that the monthly average duty-paid quantity of cigarettes in March and April 2009 decreased by 77% as compared with that of January and February 2009. For the same period in 2008, a decrease of 88% was recorded. It has been common for tobacco traders to increase their stock of duty-paid cigarettes before the Budget. As a result, the quantity of duty-paid cigarettes usually drops significantly in the one or two months after the Budget. It is therefore not appropriate to draw any conclusion from the figures at this stage.

7. The wholesale and retail prices of cigarettes, as well as the profit margin enjoyed by newspaper stallholders in selling cigarettes, are determined by the market. It is not appropriate for the Government to intervene. However, as we have pointed out during the meeting of the Bills Committee held on 21 May 2009, we will consider relaxing some operation restrictions of licensed newspaper stallholders to increase their sources of income, provided that this will not have negative impact on health and the environment.

Increase in Resources for Smoking Cessation and the Use of Smoking Cessation Services

8. The provision for publicity and education programme on smoking prevention and cessation for 2009-10 will be \$33.7 million (\$11.5 million for the Hong Kong Council on Smoking and Health (COSH), \$17.2 million for Tobacco Control Office (TCO), \$5 million for the Tung Wah Group of Hospitals (TWGHs) programme mentioned below).

9. In 2009-10, the TCO of the Department of Health (DH) will strengthen publicity, health education and promotional activities on tobacco control through TV and radio announcements in public interest, giant outdoor advertisements, health education materials, seminars and interactive online programmes on TCO website targeted at adolescents. These activities will enhance public support for a smoke-free environment and smoking cessation. In parallel, COSH will focus its efforts on promotion of smoking cessation, at the same time encouraging non-smokers to support smoking family members or friends to quit smoking. It will continue its education and publicity efforts at kindergartens, and primary and secondary schools through health talks and theatre programmes. The aim is to encourage students to say no to smoking and to support actively a smoke-free environment. COSH will also launch a new announcement of public interest to promote the importance of a smoke-free Hong Kong to the general public and to encourage smokers to quit smoking.

10. To strengthen its efforts on smoking prevention and cessation, DH has entered into a funding and service agreement with TWGHs for provision of a 3-year pilot community-based smoking cessation programme which has commenced since January 2009. The annual provision for the TWGHs programme is \$5 million. The programme covers a comprehensive range of activities and services including smoking cessation service, education for the public, training for healthcare professionals and research projects. Four smoking cessation centres are established throughout the territory to provide free smoking cessation services. To instil a smoke-free culture among the youth and young smokers, smoke-free educational programmes will be organised in collaboration with primary and secondary school principals and parents. There will also be tailor-made smoking cessation programmes for young smokers.

11. The smoking cessation hotlines operated by DH (including the TWGHs smoking cessation programme funded by the DH), the Hospital Authority, as well as the University of Hong Kong have all recorded a significant

increase in the number of calls received since the Financial Secretary's announcement of the tobacco tax increase by 50% in his Budget speech on 25 February. According to DH and TWGHs, the daily average number of callers seeking smoking cessation information increased six-fold from 24 (between January to 25 February 2009) to 141 persons (between 26 February to end March 2009). Among these, the total number of calls made by youngsters aged below 20 increased from 6 to 40 on a daily basis, representing an increase of over 400%. Indeed the total number of calls handled between 26 February to end March (4,782) has already exceeded that handled in the entire year of 2008 (4,335).

12. The daily average number of enquiries received by Hospital Authority's Smoking Counselling and Cessation Programme increased from 13 (between January to 25 February) to 46 (between 26 February to end March), representing a 350% increase. As for the Youth Quitline run by the University of Hong Kong, the total number of calls increased by more than 220% from 30 (between January to 25 February) to 98 (between 26 February to May).

13. These encouraging statistics have confirmed our assessment that the increase in tobacco tax is a strong impetus for smokers to quit smoking. The Administration will continue to enhance its smoking cessation services in future to help more smokers do so.

Social and Economic Impacts of the Proposed Cigarette Duty Rates Increase

14. As with the formulation of other policies, the proposed increase in tobacco duty has been made having considered different relevant factors including the social impact and the effectiveness of the proposal.

15. International and local researches have both pointed out that cigarette price is a key factor influencing tobacco consumption and smoking prevalence. World Health Organization's (WHO) Framework Convention on Tobacco Control which took effect in 2005 clearly points out that "the Parties recognize that price and tax measures are an effective and important means of reducing tobacco consumption by various segments of the population, in particular young persons." This is a scientific conclusion made by the WHO based on information provided by its contracting parties. The World Bank has also published a report in 1999, pointing out that, on average, a price increase of 10% is expected to reduce demand for cigarettes by about 4% in high-income countries and by about 8% in low- and middle-income countries. The Chicago University has also published its findings on a nation-wide research, revealing that

a price increase of 10% is expected to bring about a reduction in the population of young smokers by over 6% and a reduction of adult smokers by about 3% to 5%.

16. In Hong Kong, government statistics also show that the smoking prevalence rate (the proportion of daily cigarette smokers among the population aged 15 and above) fell every time after a significant tax increase:

- after a 300% increase in tobacco tax in 1983, the smoking prevalence rate dropped to 18.7% in 1984, down from 23.3% in 1982; and
- after a 100% increase in tobacco tax in 1991, the smoking prevalence rate dropped to 14.9% in 1993, as compared to 15.7% in 1990.

17. Furthermore, the economic implications of the proposed duty increase has been set out in the Legislative Council brief on the Bill. The paper points out that the proposal may lead to an increase in the retail prices of cigarettes and therefore a reduction in their consumption in Hong Kong. The resultant impact on the consumer price inflation will be minimal, due to the very small weighting of cigarettes in the basket of goods and services covered by the Composite Consumer Price Index (CCPI).

Yours sincerely,



(Ms Joan Hung)

for Secretary for Financial Services
and the Treasury

c.c.

SFH (Attn:Ms Anita Chan)

C for C&E (Attn:Mr CK Chow

Mr Albert Ho)

DoJ (Attn: Ms Betty Cheung)