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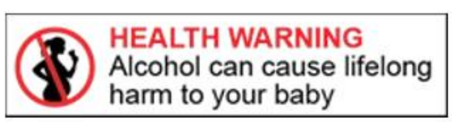
Minister Briefing

Proposal P1050 - **Pregnancy Warning Label** standard **-** approved by FSANZ Board

The implications of the FSANZ proposal may put up to 30 small New Zealand distilleries in severe financial stress, impacting upon the speed of growth of the lucrative NZ spirits industry.

The spirits industry has struggled to become established in New Zealand

- Globally distilled spirits are a US$35.2b trade earner, proven to generate jobs, economic growth and significant tax revenue in the countries where they are produced.
- In 2012, MBIE identified that NZ's spirits industry was in the top three NZ sectors well positioned for further growth, with future exports potentially worth US$282m. However, by 2016 NZ spirits exports had reduced by 50% from 2010 levels to just US$22.6m.
- Compared to other countries with related economies, the NZ industry has been slow to gain momentum.
  - Effective growth has only been in the last 4 years. Approximately 75 distilleries are currently operating in NZ, with more than 50% of these less than 4 years old, and one third opening within the last 3 years.
  - Set-up is capital intensive ($300,000-$3.5m set-up, $130,000 /year for expansion capital works) and initially intensely cashflow-negative (profit to the distiller as low as $5 / 700ml bottle) with low-to-no economies of scale.
  - The financial burden on New Zealand distilleries is forward-stacked, with many initially successful start-ups already ceasing trading due to financial difficulties.
- The difficulties in establishing a successful spirits industry is recognised globally, and many peer countries provide financial relief to their smaller distilleries in order to stimulate growth, e.g. (i) Australia provides 100% rebate for the first A$100,000 paid in excise tax, (ii) USA reduces excise tax rate for smaller distilleries by 80%. In real terms this means that USA distillers pay US$0.43 (NZ$0.67) tax for a 700ml bottle of 40% spirits, compared to NZ distillers paying NZ$15.31 excise tax for the same product.
- NZ products are significantly disadvantaged against imports within NZ, and on the export market.



Unreasonable cost burden on small NZ distilleries, putting up to 30 distilleries in financial risk

- All the mandated elements chosen by FSANZ make it the most expensive option possible. FSANZ estimated there would be a total cost to Aus/NZ industry of A$611m (worst case) for one label change.
- The FSANZ estimate included a distillery cost of A$7,575 per label to change over. FSANZ generalised that smaller business mostly use digital printing and would have lower costs and find it easier to change.
- The key point missed by FSANZ is that there is no free cashflow buffer in small new distilleries in NZ to replace labels which are only a few year's old. In the first 3-4 years of operation typically all profits go back into the business; the distiller does not earn a salary and dividends are not paid. The distillery is on the knife edge of success/ failure.

Multiple changes over at least 3 years

- There could be up to 4 upcoming changes to labels in the next 3 years (pregnancy, added sugar, carbohydrate content and nutrition panel information, container deposit/return scheme).
- A distillery with 5 SKUs could, in worst case, be impacted by 20 label changes (NZ$158,000) over 3 years.
- Many distilleries would have more than 5 SKUs; some distilleries would have more than 15.
- In most cases the back label will need to become bigger to accommodate all the mandated information (extra cost of new knife guides, redesign of total bottle label combination).
- If extra colours are used, the increased costs per label would be ongoing beyond the first redesign cost. The ongoing cost of adding 3 extra colours to a screen-printed label is up to $0.60 a bottle depending on volumes ordered. Three new colours could represent an on-going loss of profit of 12% per bottle.
- For a small producer, the timing of transition is very difficult. It could be expected that a small distillery would save all the changes to be made until the end of the 2-year transition period when all the available mandated label changes can be done at once. However, sales may be unpredictable for new brands, and large amounts of label stock may be in storage. Change is more likely to be when a batch is used up, in order to minimise packaging write-offs.
- Many distilleries use premium printed glass bottles imported from overseas, and there are large minimum order sizes. This could represent 6 months – 1 year stock.
- FSANZ estimates that 50% of SKUs could be combined with other label changes within the proposed 2-year transition period and would on average reduce costs per SKU by 70%.
- In order to minimise stock write-offs for smaller distillers, a 3-year year transition period would provide a more realistic buffer to capture the upcoming multiple changes.

The FSANZ Act requires FSANZ to have regard to whether costs that would arise from the regulatory measure outweigh the direct and indirect benefits to the community, government or industry that would arise from the proposed measure (paragraph 59(2)(a) of the FSANZ Act).

This is a far more prescriptive warning label than is required by Australia New Zealand Food Standards Code:

- The Code (Standard 1.2.3) only requires a warning statements **to be legible and prominent to contrast distinctly with the background of the label.** Font size 3 mm for larger packages is required but red colour is not mandated, only a contrast colour.
- All other FSANZ mandatory warning statements, including those used for food harmful to developing foetuses (soft cheeses, pate, certain fish, etc), do not require the excessive combination of bold text, borders, 3mm of clear space, mandated colours or wording.
- Most international jurisdictions call only for contrast and not specific colours; none of the 13 countries with pregnancy warning labels prescribe this particular combination of design elements. Only Turkey, of the 11 countries, requires the colour red.

New Zealand distillers are not against a mandated label – but the implications of the FSANZ proposal may put up to 30 small NZ distillers in severe financial stress, impacting upon the speed of growth of the lucrative NZ spirits industry.

Requests:

1. Do not mandate red, black and white - allow for any colour to be used with a contrasting background to highlight the label (as per the Australia New Zealand Food Standards Code).
2. Lengthen the transition to 3 years, acknowledging that the multiple upcoming mandated label changes need to be coordinated.