



This material was produced by The International Union Against Tuberculosis and Lung Disease and is now supported by the Tobacco Control Division of Vital Strategies.

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## Factsheet 1.

# Tobacco taxation

# 01

Boys smoking in Indonesia. Young people are the most likely to quit when tobacco prices rise. Credit: Damien Schuman

Increasing tax on tobacco is the most effective way to reduce tobacco consumption. It is high-impact and cost-effective.<sup>1</sup> When used strategically, increased tobacco taxes can help to cover the cost of tobacco use to a society, and the extra revenue from the tax can be dedicated for health promotion.<sup>2</sup>

The Philippines offer an exemplar of this kind of strategy: in 2012 the government raised tobacco taxes. The following year, projected revenues from this tax increase exceeded expectations. The additional funds will be invested in improvements to health facilities nationwide, and in universal health coverage.

### Tobacco tax can be applied in two ways:<sup>3</sup>

1. Specific tax – a fixed amount added to the price of the tobacco product.
2. Ad valorem or value-added tax – calculated as a percentage of the base price of the tobacco product.

These two taxes can be used in combination to great effect: ad valorem maintains tobacco prices in line with inflation, and specific taxes provide predictable revenue and make it harder for the tobacco industry to influence retail prices.

### Tobacco taxation reduces consumption because price increases:

- Encourage people to quit
- Prevent people from starting smoking
- Discourage ex-smokers from starting again<sup>4</sup>

### For example:

- When tobacco tax rates were increased by 250% in South Africa during the 1990s, cigarette consumption fell by 5-7% for every 10% increase in cigarette prices. Approximately 40% of the decline in consumption was due to smokers quitting.<sup>5,6</sup>

- Egypt increased tax in 2010 which led to a decrease in sales by 14% in 2 years.<sup>7</sup>
- Turkey increased tax in 2010. In conjunction with other policies this led to a decrease in sales and decreased the number of smokers.<sup>8</sup>

Increasing tobacco taxes has a greater impact on consumption in low- and middle-income countries. A price rise of 10% decreases consumption by up to 8% in low- and middle-income countries and by 4% in high-income countries.

### Status of taxes as tobacco control policy

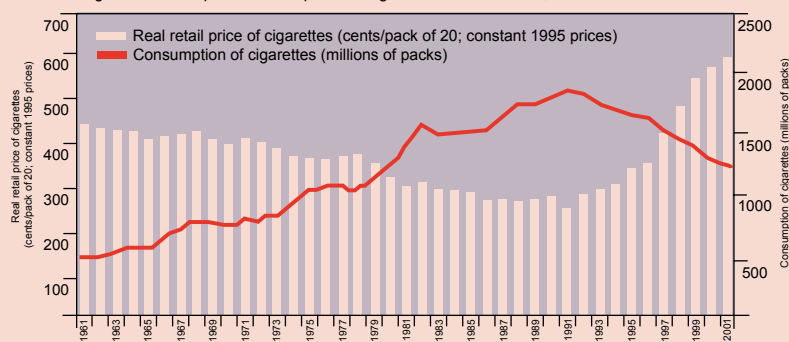
Currently, just 8% of the world's population live in countries with sufficiently high tobacco taxes; therefore there is great scope for using tax to reduce tobacco consumption globally.<sup>7</sup> And in many countries cigarette prices have not kept up with inflation, or the price increases of other goods and services.<sup>9</sup>

Tripling tobacco taxes worldwide would increase tobacco prices by 70% and would prevent 115 million tobacco-related deaths by 2050. The most lives saved would be young men in low- and middle-income countries.<sup>10,11</sup>

## Key Facts

- Increasing tobacco prices through taxation is the most effective way to reduce tobacco consumption.
- The tobacco industry strongly opposes tax increases because it is such an effective tobacco control measure.
- Increased revenues from higher tobacco taxes can be used to reduce consumption still further, when the new funds are dedicated for use in tobacco control programmes.
- Higher tobacco taxes can prevent death and malnutrition by reducing the proportion of household income spent on tobacco rather than on food.
- Young people, and those with low income, are the most likely to quit when tobacco prices rise.<sup>12</sup>
- Article 6 of the WHO Framework Convention on Tobacco Control [WHO FCTC] states that parties must consider tobacco control objectives when setting tax policies.

Cigarette consumption and real prices of cigarettes in South Africa, 1961 to 2001



From C van Walbeek. Tobacco Excise Taxation in South Africa, WHO, 2003.

## Countering tobacco industry myths about taxation

The tobacco industry almost always strongly contests higher tobacco taxation because it is such an effective tool for reducing consumption. It frequently uses the following arguments:

### ***'Tobacco taxation leads to loss of revenue'***

In fact, when tobacco taxes rise, tax revenues tend to rise.<sup>12</sup>

For example, in 1994 Canada reduced tobacco taxes in an attempt to recover revenue lost to smuggling tobacco products. They were encouraged to do so by the tobacco industry.<sup>13</sup> One year later tax revenues had fallen significantly and cigarette consumption had increased.

### ***'Increased tobacco taxation leads to increased illicit trade'***

Until recently the highest levels of illicit tobacco trade in Europe were found in countries with the lowest tobacco taxes.<sup>7</sup>

#### **For example:**

In the mid 1990s Spain had low cigarette prices and large-scale cigarette smuggling. By 2002 tobacco prices had doubled, and smuggling had fallen from 14.5% of the market in 1994, to just under 2%. Tax revenues also rose by 155% during that period. Spain used a multi-pronged approach to tackle smuggling - through intelligence, customs and excise reform, new technology and cooperation with other EU countries.

This illustrates how weak governance, customs and excise administration, corruption and the complicity of cigarette manufacturers allow illicit tobacco trade to flourish.<sup>14 15 7</sup>

### ***'Increased tobacco taxation is unfair to the poor'***

People with a low income are more price-sensitive than those on a comparatively high income. They are therefore more likely to stop smoking or reduce consumption when faced with a tobacco tax increase that affects price. This has a beneficial impact on health, both for the quitter and their family, as funds previously spent on tobacco are freed up. In Bangladesh, for example, half of the children who are dying from malnutrition could be prevented from dying if their household income was spent on food instead of cigarettes.<sup>16</sup> Tax increases in combination with other tobacco control measures would help to achieve this.

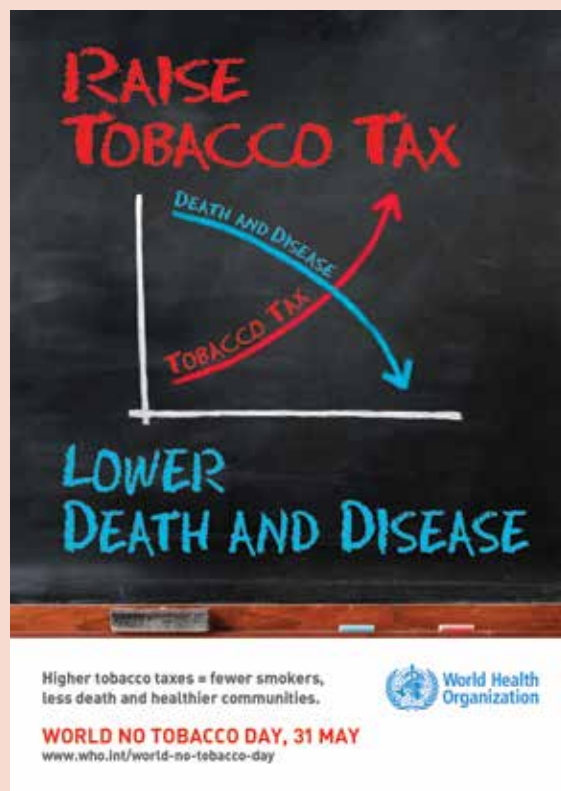
There is also evidence that tobacco tax increases are progressive in the longer term, shifting the tax burden from the poor to the rich.<sup>10</sup> The largest decline in South African cigarette consumption during the 1990s was among the young and the poor when taxes increased.<sup>5</sup>

#### **WHO FCTC requirements**

Under Article 6 of the WHO Framework Convention on Tobacco Control, parties must:<sup>17</sup>

- Consider tobacco control objectives when setting tax policies.
- Recognise that price and tax measures reduce tobacco consumption, especially among the young.

A new protocol on illicit trade is now being negotiated that will combat smuggling and counterfeiting of tobacco products.<sup>18</sup>



World Health Organization poster for World No Tobacco Day 2014

## Best practice

- Set the tax at between two thirds and four fifths of the total retail price on all tobacco products.
- Apply the taxes at manufacturer level and have them certified by a stamp.
- Apply the same taxes to imported cigarettes as to domestically manufactured cigarettes.
- Tax all tobacco products at comparable rates to prevent product substitution.
- Tie the tobacco tax to the rate of inflation and consumer purchasing power.
- Allocate tobacco tax revenues, or a portion of them, to tobacco control or health promotion programmes.
- Ban the 'duty free' sale of tobacco products.
- Keep taxes simple and easy to implement.

# References



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