Taxes levied on Cigarettes

By
Ayda A. Yurekli, PhD.
Program Leader,
Research for International Tobacco Control (RITC) at
International Development Research Center (IDRC),
Ottawa, Canada
Content

- Types of taxes levied on cigarettes
  - Tax structure
  - World wide Excise application

- Advantages and disadvantages of types of excise

- Impact of types of excises on retail price

- Over view on tax and average retail price of cigarette levels by income group countries and regions
Types of taxes levied on tobacco products

- Consumption Tax
  - Sales tax
  - General Sales tax
  - Turnover tax
- Import Duty
  - Excise tax
  - VAT
    - Specific tax
    - Ad Valorem tax

Source: Yurekli & Onder 2005
Structure of Excise Taxes

- Specific: tax base is physical unit (e.g. per kilo or per stick)
- Ad valorem: tax base is value of sales (e.g. percentage of wholesale or retail price)
- Specific & Ad valorem Taxes: Combination of both excises
### Excise System by Region & Income groups

<table>
<thead>
<tr>
<th>By Income</th>
<th>Only Specific</th>
<th>Only Ad-Valorem</th>
<th>Specific &amp; Ad-valorem</th>
<th>No Excise</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>High</td>
<td>9</td>
<td>0</td>
<td>22</td>
<td>5</td>
<td>36</td>
</tr>
<tr>
<td>Upper-Middle</td>
<td>4</td>
<td>12</td>
<td>11</td>
<td>43</td>
<td>30</td>
</tr>
<tr>
<td>Lower-Middle</td>
<td>15</td>
<td>25</td>
<td>14</td>
<td>5</td>
<td>34</td>
</tr>
<tr>
<td>Low</td>
<td>8</td>
<td>19</td>
<td>1</td>
<td>5</td>
<td>34</td>
</tr>
<tr>
<td>By Region</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>TOTAL</td>
</tr>
<tr>
<td>Africa</td>
<td>6</td>
<td>19</td>
<td>1</td>
<td>7</td>
<td>33</td>
</tr>
<tr>
<td>N.America</td>
<td>2</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>2</td>
</tr>
<tr>
<td>EU</td>
<td>1</td>
<td>0</td>
<td>26</td>
<td>0</td>
<td>27</td>
</tr>
<tr>
<td>ECA</td>
<td>9</td>
<td>5</td>
<td>5</td>
<td>0</td>
<td>19</td>
</tr>
<tr>
<td>LAC</td>
<td>3</td>
<td>19</td>
<td>2</td>
<td>0</td>
<td>24</td>
</tr>
<tr>
<td>MENA</td>
<td>2</td>
<td>4</td>
<td>2</td>
<td>10</td>
<td>18</td>
</tr>
<tr>
<td>SA</td>
<td>2</td>
<td>3</td>
<td>0</td>
<td>0</td>
<td>5</td>
</tr>
<tr>
<td>EAP</td>
<td>12</td>
<td>5</td>
<td>6</td>
<td>7</td>
<td>30</td>
</tr>
<tr>
<td>TOTAL</td>
<td>37</td>
<td>55</td>
<td>42</td>
<td>24</td>
<td>158</td>
</tr>
</tbody>
</table>

IDRC: (24%)  CRDI: (35%)  Canada: (26%)  MENA: (15%)
Most HI Countries rely more on Ad-Valorem excise

Source: Yurekli & Onder 2005
Lower-Middle Income rely more on Ad-Valorem while Upper-Middle Income balance both excises

Source: Yurekli & Onder 2005
Advantages of Excises

Specific Excises

- Simplicity
  - Tax liability easy to measure
  - Taxes prepaid on sales

- Health benefits
  - External costs of smoking same for high and low price brands – tax rate should be the same

Ad Valorem Excise

- Tax liability Indexed to cigarette price inflation
- Discourages substitution from low-price to high-price brands – and so generates higher revenues
- Discourages investment in advertising to make smoking “glamorous”
Disadvantages of Types of Excises

Specific Excise
- Revenues do not increase automatically with inflation
- Encourages improving “quality” of cigarettes
- Encourages substitution to (high-price) imported brands; or smuggled-tax free low-quality alternatives
- Increases potential for tax avoidance and revenue loss if tax base set on characteristic of cigarettes (e.g. weight, content, size of cigarettes)

Ad Valorem Excise
- Difficult to collect at retail points of sale
- Creates potential for tax avoidance and revenue loss
- Smaller health benefits than equivalent specific tax
Types of Excises and Their Impact on Average Retail Price
Average price by Excise Type in High Income Group Countries

HIGH INCOME COUNTRIES 2004-2005

- **Average Price**
- **Average Excise/pack**
- **% of Excise**

<table>
<thead>
<tr>
<th>Excise Type</th>
<th>Average Price</th>
<th>Average Excise/pack</th>
<th>% of Excise</th>
</tr>
</thead>
<tbody>
<tr>
<td>Both Excises</td>
<td>$3.57</td>
<td>$2.14</td>
<td>60%</td>
</tr>
<tr>
<td>Specific Dominates Ad Valorem</td>
<td>$4.83</td>
<td>$2.93</td>
<td>61%</td>
</tr>
<tr>
<td>Ad Valorem Dominates Specific</td>
<td>$2.99</td>
<td>$1.77</td>
<td>59%</td>
</tr>
<tr>
<td>Specific Only</td>
<td>$4.82</td>
<td>$2.63</td>
<td>55%</td>
</tr>
</tbody>
</table>

Source: Yurekli & Onder 2005
Average price by Excise Type in Low Income Group Countries

LOW INCOME COUNTRIES 2004-2005

<table>
<thead>
<tr>
<th>Average Price</th>
<th>Average Excise/pack</th>
<th>% of Excise</th>
</tr>
</thead>
<tbody>
<tr>
<td>Specific Only</td>
<td>$1.38</td>
<td>$0.26</td>
</tr>
<tr>
<td>Ad Valorem Only</td>
<td>$0.73</td>
<td>$0.21</td>
</tr>
</tbody>
</table>
### Average price by Excise Type in Middle Income Group Countries

#### MIDDLE INCOME COUNTRIES 2004-2005

<table>
<thead>
<tr>
<th>Type</th>
<th>Lower Middle Income</th>
<th>Upper Middle Income</th>
</tr>
</thead>
<tbody>
<tr>
<td>Specific Only</td>
<td>$1.09</td>
<td>$1.25</td>
</tr>
<tr>
<td>Ad Valorem Only</td>
<td>$1.07</td>
<td>$1.33</td>
</tr>
<tr>
<td>BOTH</td>
<td>$1.08</td>
<td></td>
</tr>
</tbody>
</table>

- Average Price
- Average Excise/pack
- % of Excise

Source: Yurekli & Onder 2005
Tax and Price Structure of Cigarettes by Income Group and Regions
Average price US$/pack
Average price PPP/pack
Total tax %
Excise tax %

<table>
<thead>
<tr>
<th>Category</th>
<th>Average price US$/pack</th>
<th>Average price PPP/pack</th>
<th>Total tax %</th>
<th>Excise tax %</th>
</tr>
</thead>
<tbody>
<tr>
<td>HI</td>
<td>$3.62</td>
<td>$3.74</td>
<td>68%</td>
<td>49%</td>
</tr>
<tr>
<td>UMI</td>
<td>$2.49</td>
<td>$1.35</td>
<td>55%</td>
<td>36%</td>
</tr>
<tr>
<td>LMI</td>
<td>$2.73</td>
<td>$1.33</td>
<td>48%</td>
<td>26%</td>
</tr>
<tr>
<td>LI</td>
<td>$2.83</td>
<td>$0.71</td>
<td>42%</td>
<td>21%</td>
</tr>
</tbody>
</table>
Conclusion

- Cigarettes are taxed by all countries though.
  - Import duties by all countries - for imported cigarettes
  - Consumption taxes by most countries
    - Sales or value added taxes (VAT)
    - Excise taxes

- It is important to understand the strength and weaknesses of types of excise taxes in terms of their impact on
  - Consumption
  - Retail price
  - Revenues
  - Product improvements
  - Industry profit

- Countries should adopt & tailor excises based on their objectives and the ability of administration