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Economic Research Informing Tobacco Control Policy

Regional Tobacco Taxation

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Why integrate tobacco taxation regionally?

- Contributes to significantly less price variation across countries.
- This typically translates into less tax avoidance (e.g., cross border shopping) and tax evasion (e.g., smuggling).
- Some evidence suggests that it can be a proverbial "tide that lifts all boats."
  - Governments seek to race to the "top" by improving their tobacco tax policy even above and beyond the basic regional requirements.
- In the case of the EU, countries around it have also sought to emulate tax policy either because of EU accession (the acquis communautaire), because they see neighbours' success, or because they wish to avoid any negative implications from others organizing together.

The European Union

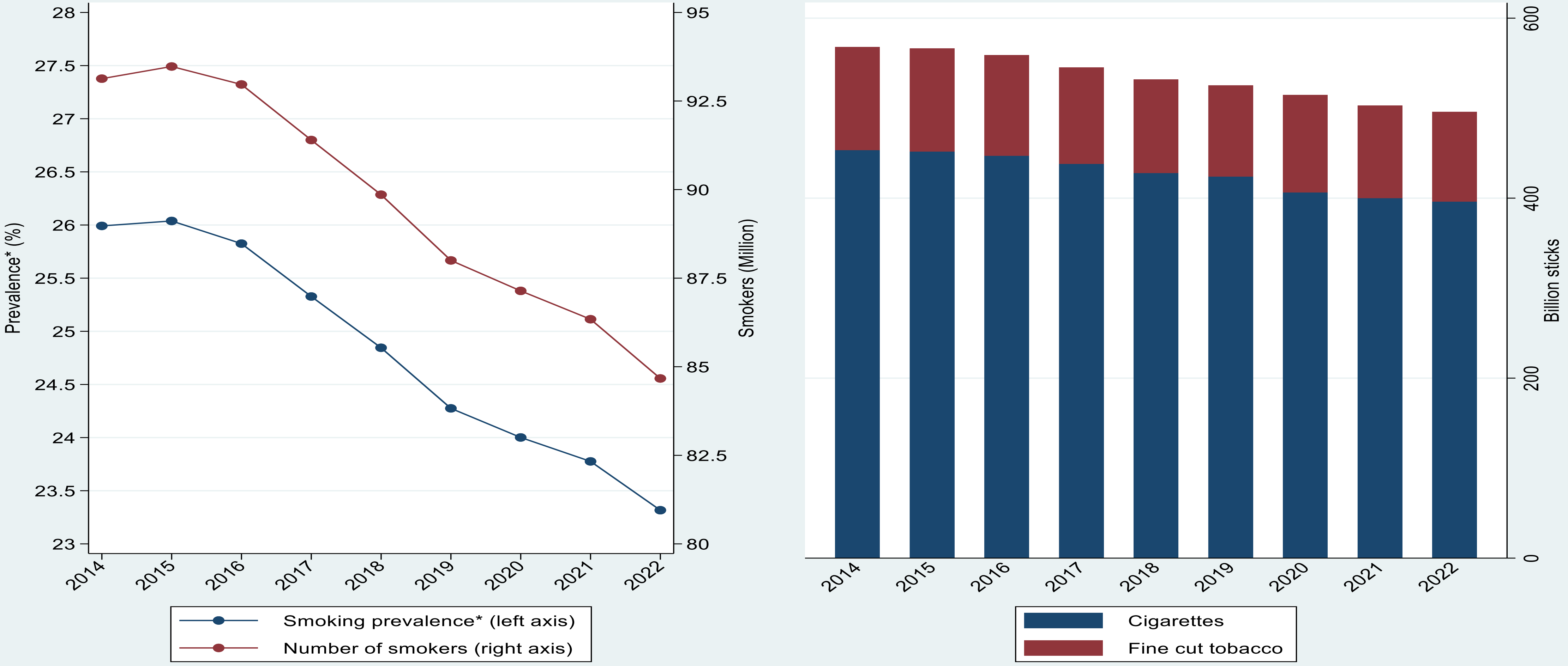
- The EU has the Tobacco Tax Directive or “TTD” for all member states.
- The tax structure must be a hybrid of specific and ad valorem taxes.
- It compels that countries meet a minimum excise tax (MET) of 90 Euro per 1000 cigarette sticks (through specific and/or ad valorem taxes).
- And the tax share of weighted average retail price must be at least 60 percent.
- Countries are permitted to go above these minimum benchmarks.
- The TTD treats other non-cigarette tobacco products with lower rates.
  - Including hand-rolled tobacco, e-cigarettes and heated tobacco products.

Tobacco taxation

- As a result of the Tobacco Tax Directive, the countries of the EU as a region have better tobacco taxation policies than most.
- Tax rates are higher than most regions and have led to typically higher prices (though it still varies across & within countries).
- The higher prices have– until recently– driven down consumption in many countries in the EU.
- Nonetheless, smoking rates remain high in some countries.

Smoking prevalence, number of smokers and market volumes

European Union



*In population of legal smoking age; population weighted average
Malta, Cyprus and Luxembourg not included
Sources: Author's elaboration with data from Euromonitor

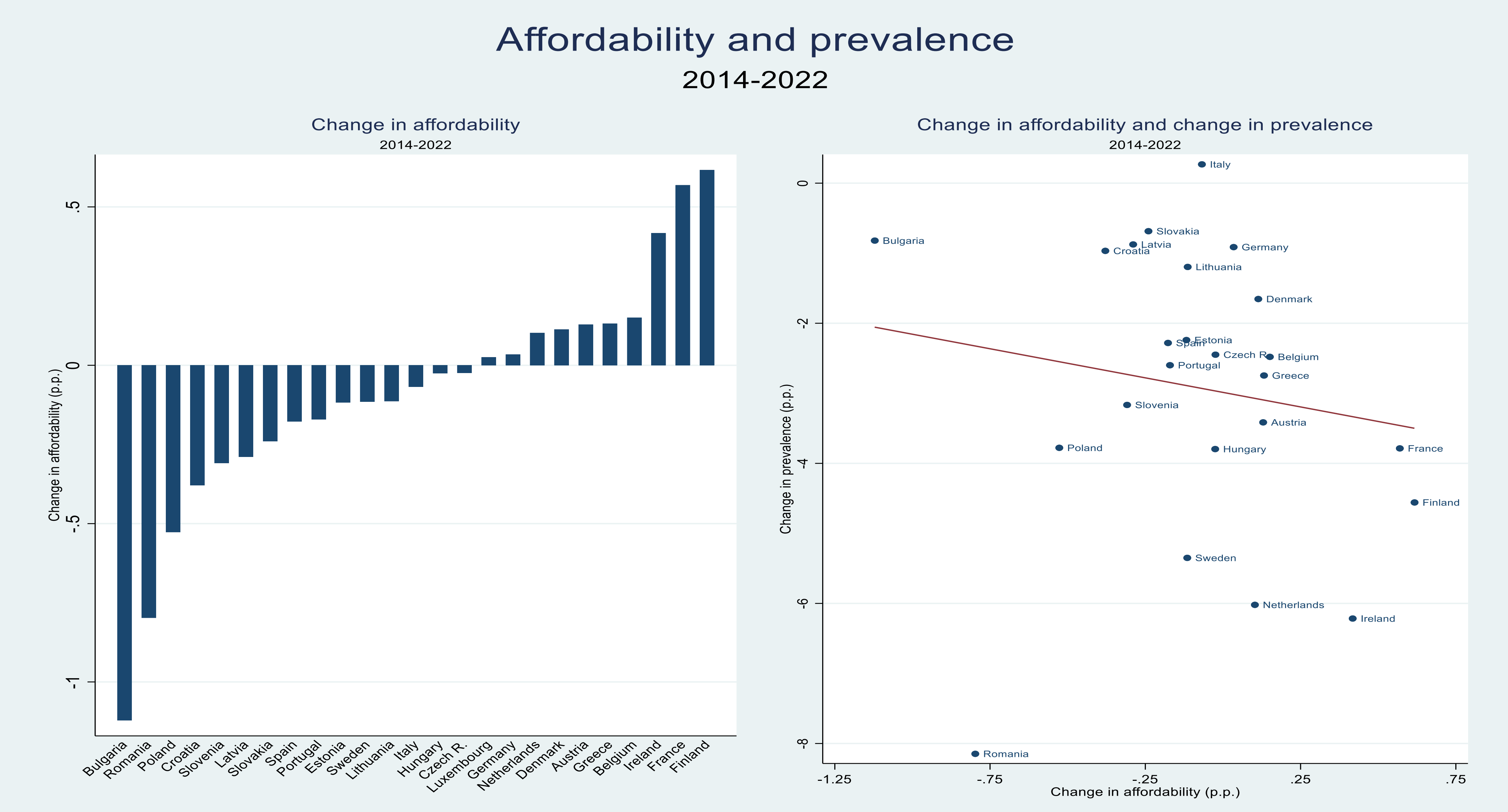
Source: Lopez, 2023

European Union supply chain control

- Another key feature of integration around tobacco taxation is an EU-wide track and trace system– member states must use it.
- All countries must be in the shared system and meet minimum operational requirements.
- All countries are compelled to share data with each other.
- It’s not perfect but it is arguably world-leading from the perspective of a larger multi-country system to control the supply chain of a major sector.

Tobacco taxation in the EU - challenges

- The Tobacco Tax Directive has not been updated in many years.
- 90 Euros per 1000 sticks is not high enough in many countries to make cigarettes less affordable.
- Realistically, to keep cigarettes from becoming more affordable, the rate needs to be around 200 Euros per 1000 sticks or more.



Affordability measured as share of expenditure per capita needed to buy 1000 cigarettes at average prices
Sources: Author's elaboration with data from Euromonitor, Eurostat and European Commission

Source: Lopez, 2023

Revising the Tobacco Tax Directive

- The European Commission recently put forward a revision:
  - The proposed rates are significantly higher but still unlikely to make cigarettes consistently less affordable.
  - It does not sufficiently address the low rates for rolling tobacco (so-called “fine-cut tobacco”).
  - It does not sufficiently address rates for “novel” tobacco products like heated tobacco products (HTPs) and e-cigarettes.

Tax floors are good…

- A tax floor of the equivalent of 90 Euros per 1000 cigarettes (like the EU's) would be a good start for many Latin American countries.
- But even such minimum benchmarks must be raised steadily.
- At a minimum, governments must adjust rates annually for inflation.
- Governments should also adjust for income growth.
  - This tends to be particularly important in middle-income countries where growth is often higher than in higher-income ones.
- But this effort will only keep tobacco products "even" with affordability.
- It is necessary to increase rates above inflation & growth to make tobacco products less affordable.

Examples from West Africa…

- Economic Community of West African States (ECOWAS) is a 15-country customs union, and the West African Economic and Monetary Union (WAEMU) is an 8-country customs and monetary union.
- Since 2017, these unions have set a minimum ad valorem tax of 50 percent (on ex-factory).
    - ECOWAS also levies a $0.02 per stick specific tax.
- However, WAEMU also sets a ceiling of 150 percent ad valorem.
    - ECOWAS previously had a ceiling but eliminated it.
- Not surprisingly, the reform had a reasonably significant effect in ECOWAS and almost none in WAEMU.
- There is no justification for this “ceiling” on tobacco tax other than to protect the tobacco companies and is a tobacco taxation “worst” practice.

What next?

- Beyond the EU, Latin America has one of the stronger records of regional economic integration (e.g., Mercosur), so there are strong precedents for such a regional tobacco tax initiative.
- Equalizing higher taxes across countries in the region would significantly raise tax revenues and drive down smoking rates.
  - It would likely mitigate tobacco tax avoidance and evasion
- Health costs would decrease, and economic productivity would increase across the region.
- Implementing track and trace systems that share information among neighbours will drive down the number of illicit products.

So, what could go wrong?

- The political economy of integrated tobacco taxes is complex.
- Tobacco companies everywhere are economically and politically large and strong.
  - These actors mostly view organized multi-country taxes as a quasi-existential threat and will inevitably push back very hard on them.
- They choose governments that are sympathetic and/or weak to undermine these efforts.
- Since many agreements are consensus-based, parameters typically fall to the lowest common denominator.
- Ongoing discussions about regional tax can “cool” country-level efforts.

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Gracias/Obrigado/Thank you.

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