

Fiscal reform trends and opportunities of tobacco taxes

Session 4. Leveraging fiscal reforms to advance tobacco tax policy

Workshop: Advancing tobacco taxes in Latin America

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29 of October, 2024



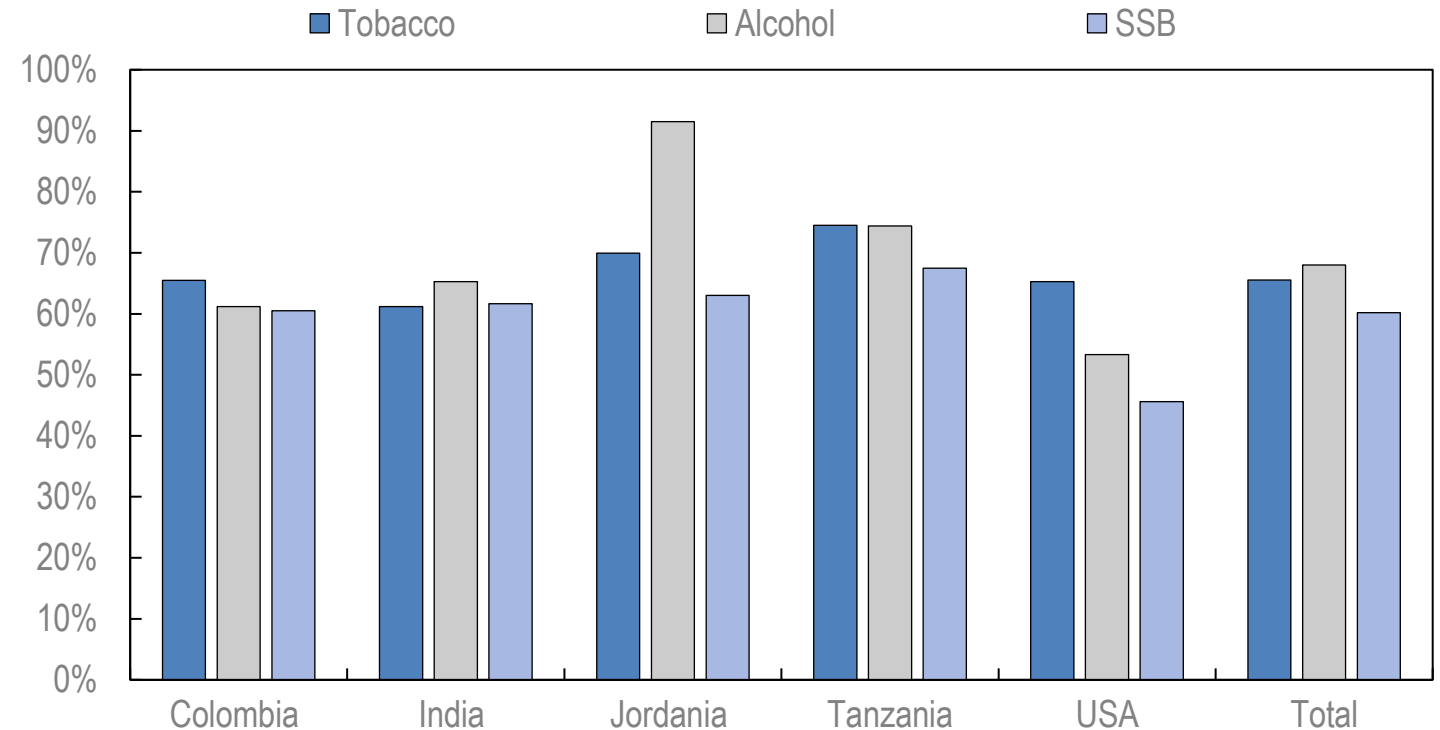


Health taxes can play a bigger role in the tax mix of countries in LAC

1. While many LAC countries must **strengthen domestic resource mobilisation** in a context of fiscal pressure....
2.they are facing **challenges** in implementing **broad tax reforms**.
3. There is **public support for raising health taxes**.
4. Health taxes are **easier to collect and administer** than other broad-based taxes.
5. **Revenue from health excise taxes** in LAC is **low** compared to other regions.

Public support for raising health taxes

Percentage of surveyed people



Source: OECD based on Gallup measuring Public Perceptions of Noncommunicable Diseases Survey, 2021-2022.

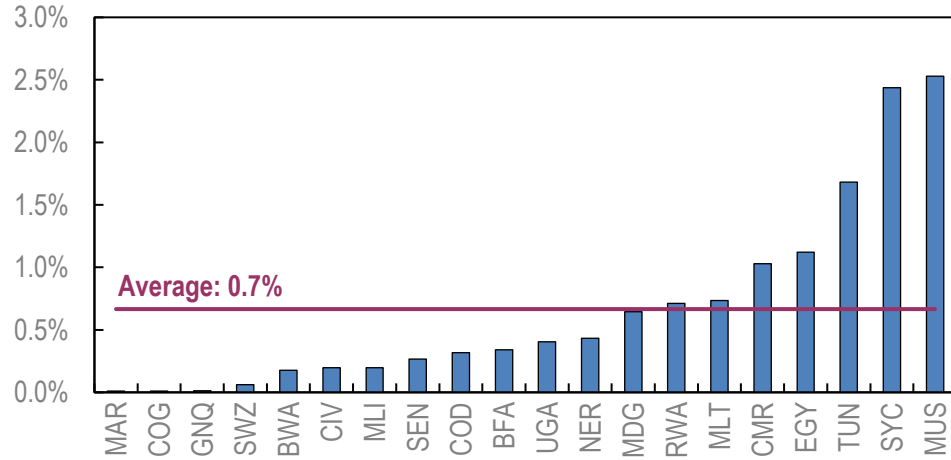


Revenue from health excise taxes in LAC is lower than in other regions

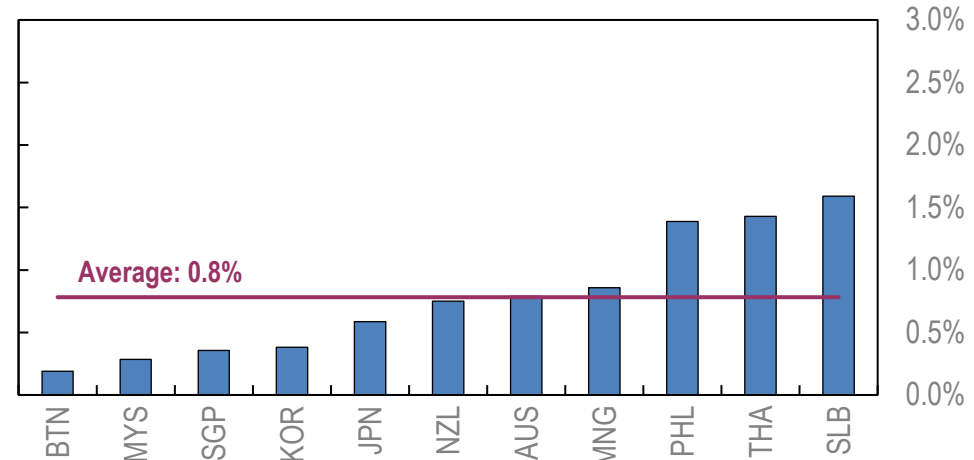
Health excise tax revenue across the world

Percentage of GDP

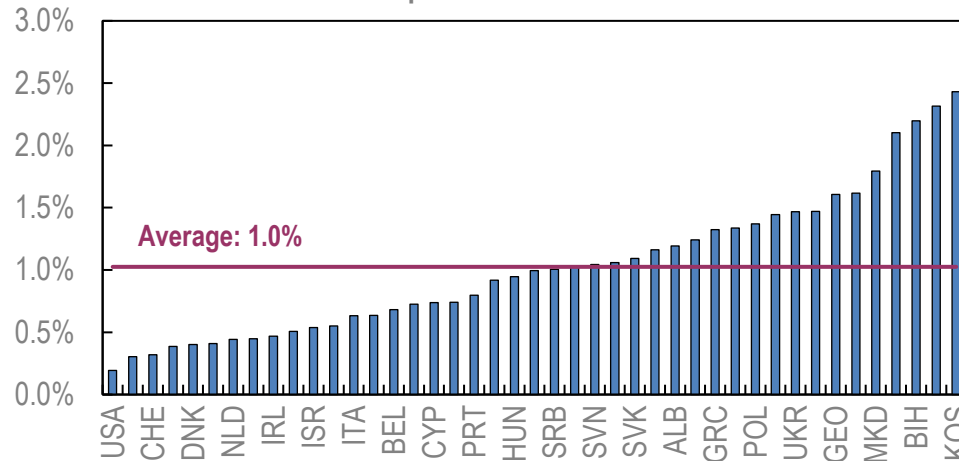
Africa



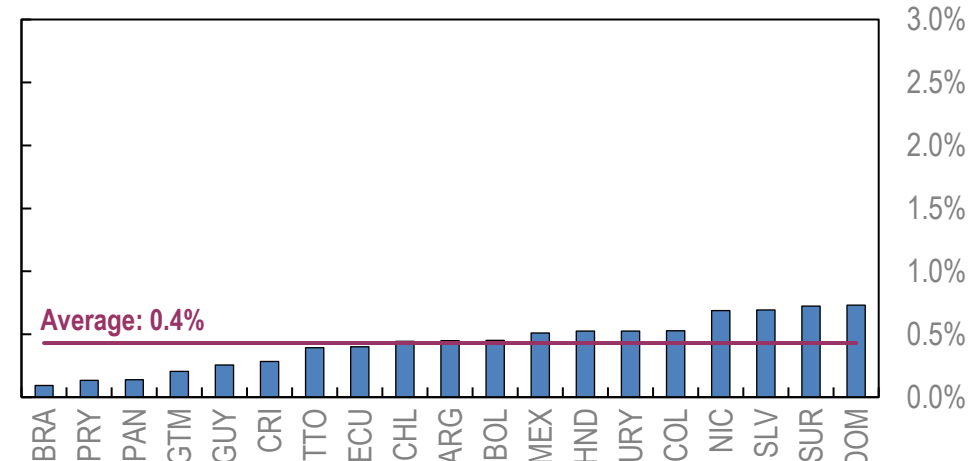
Asia



Europe & North America



Latin America & the Caribbean



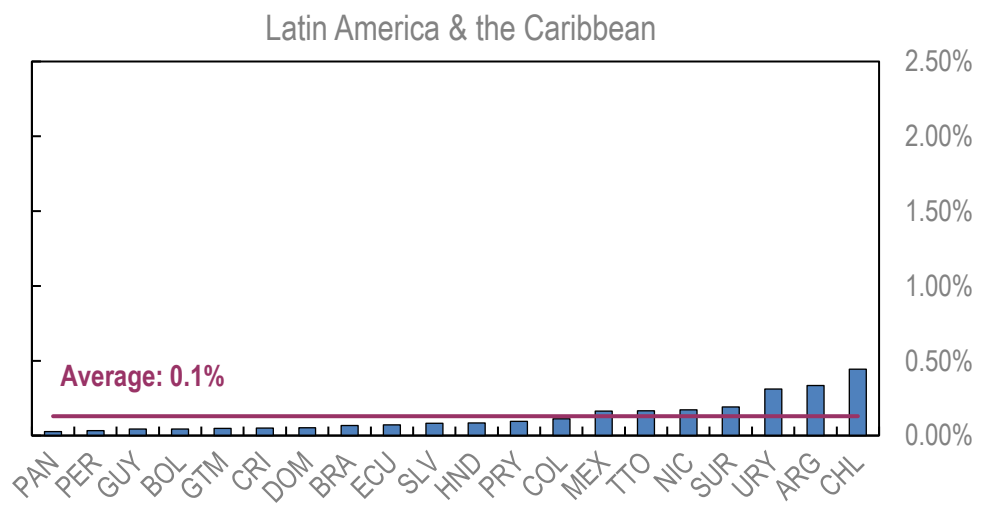
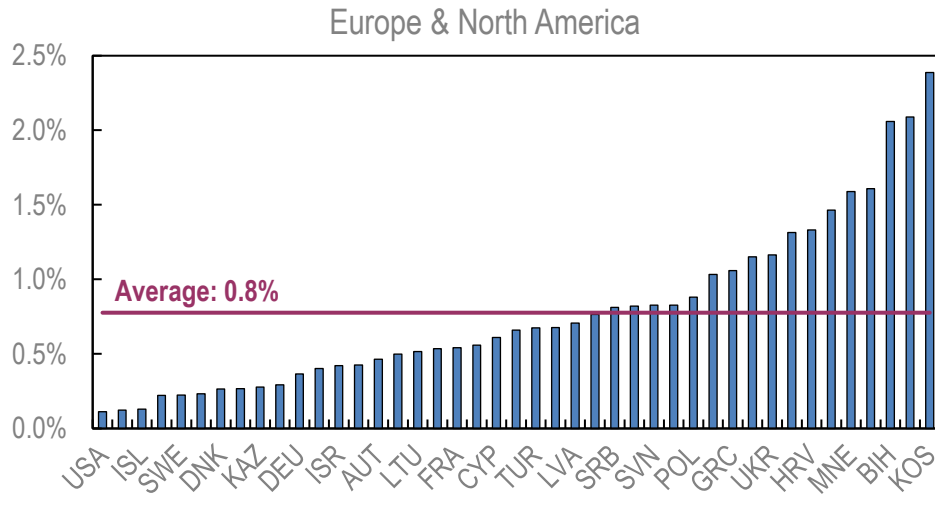
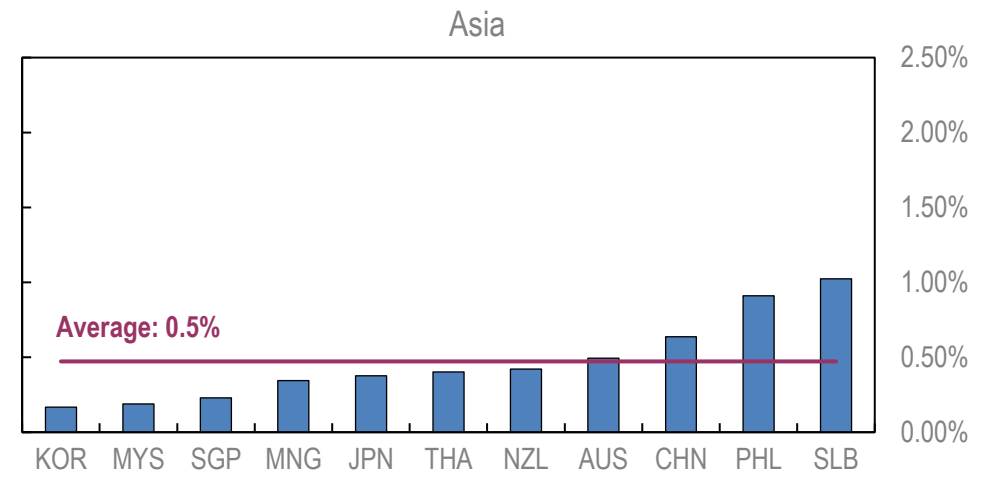
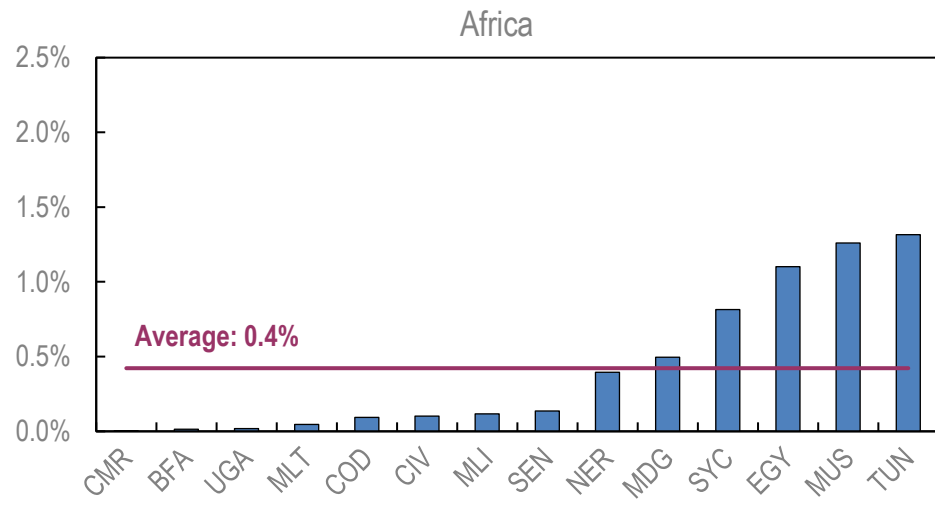
Source: OECD Global Health Tax Revenue database.



Revenue from tobacco excise taxes in LAC is lower than in other regions

Tobacco excise tax revenue across the world

Percentage of GDP



Source: OECD Global Health Tax Revenue database.



There is a need for tobacco tax reform in LAC

1. Cigarettes remain (too) affordable, which is ineffective to incentive smokers to reduce or quit smoking.
2. Tobacco tax burden is low and declining in many countries.
3. Countries are not fully tapping into their tobacco tax revenue potential.
4. The implementation of tobacco taxation is lagging behind compared to other non-tax tobacco control measures.



Tobacco tax reform priorities across countries in LAC

Regular increases of specific taxes

Increase specific tobacco excise tax levels and index them to inflation and real income growth to reduce the affordability of tobacco products.

Enhanced ad valorem taxes

Introduce a minimum tax or price floor and levy the ad valorem excise tax on the suggested or actual retail price rather than on the ex-factory price.

Similar tax burden across products

Align the design of excise taxes across tobacco products to achieve a similar tax burden, especially between highly substitutable tobacco products, to prevent smokers from trading down.

Taxing emerging products

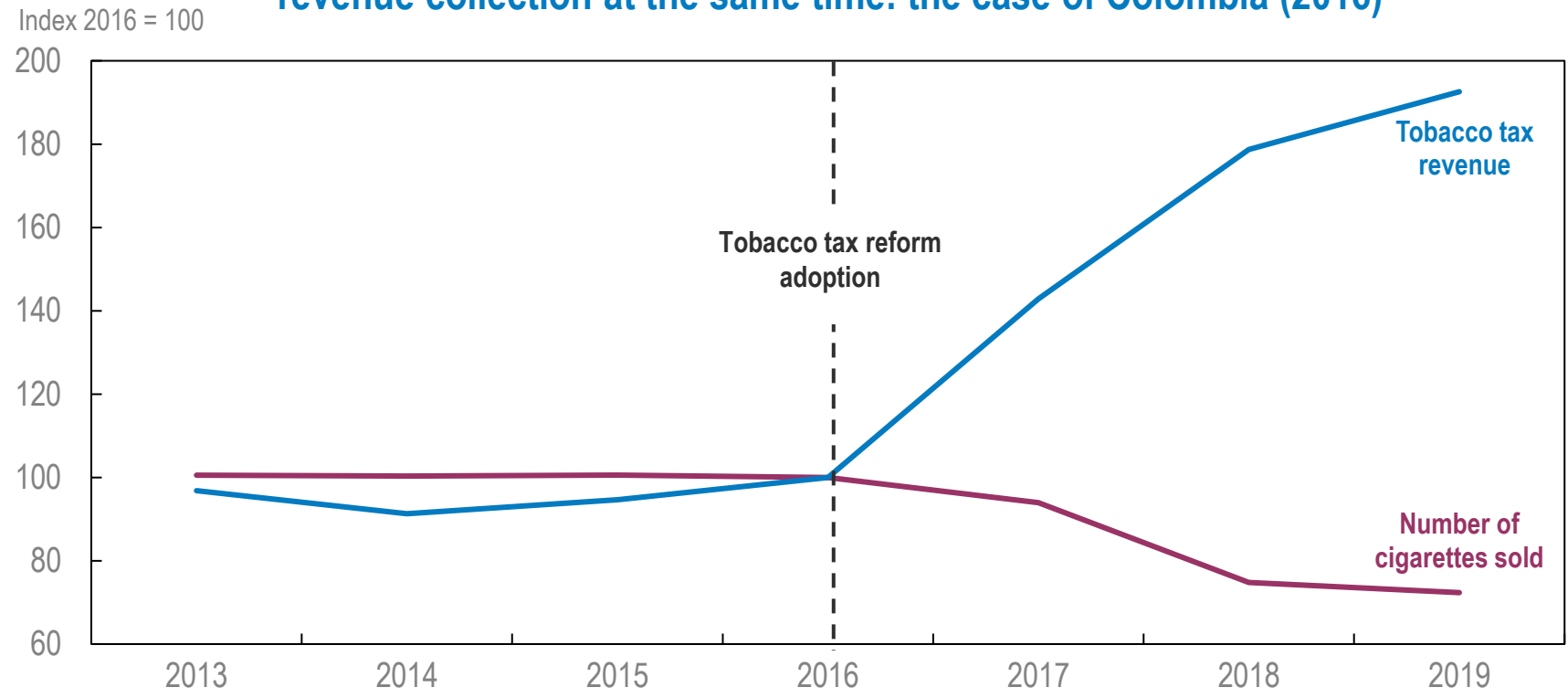
Where the sales of new emerging tobacco and nicotine products are not banned, tax them at similar levels than cigarettes to reduce their taking up, especially among young people.



Concerns on revenue loss and illicit trade should not deter tobacco tax reform (I)

- > Tobacco tax revenue will very likely grow in the short term, even if sales for tobacco products decline.
- > In the longer run, the reduction of tobacco-related costs would be far larger than the loss of tobacco tax revenue, thereby having a net positive budgetary impact.

Ambitious tobacco excise tax reform curbs tobacco consumption and strengthens tax revenue collection at the same time: the case of Colombia (2016)



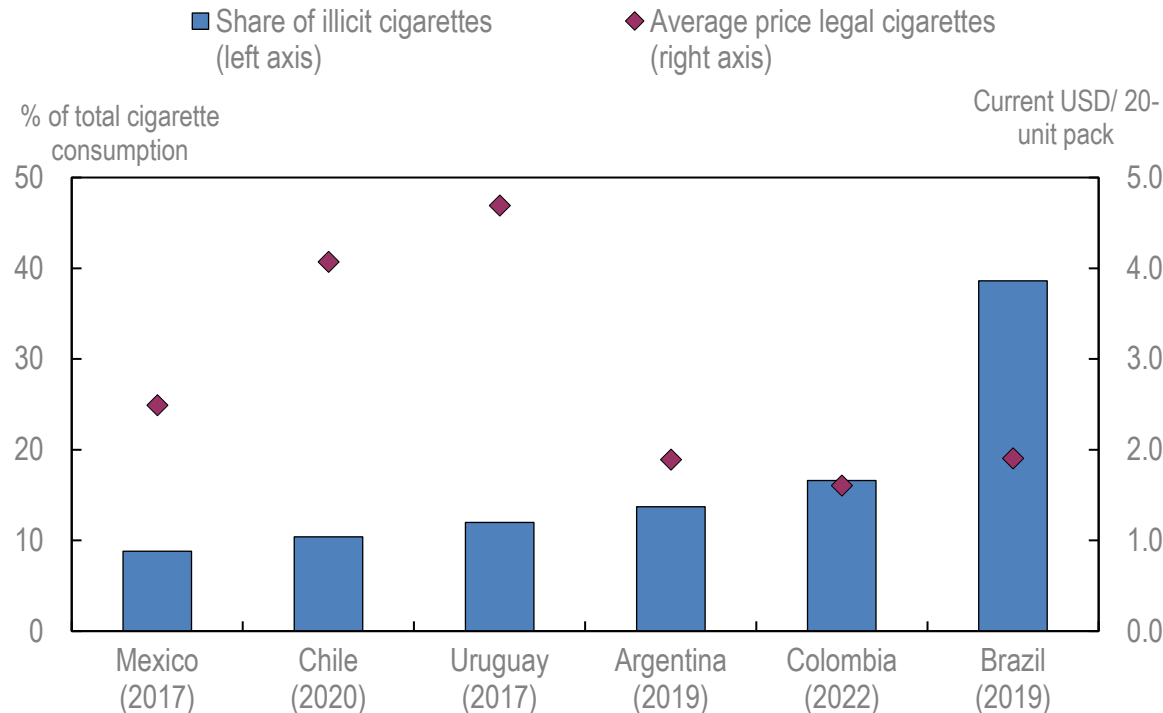
Note: Tobacco tax revenue is expressed in constant (inflation-adjusted) local currency.
Source: Ley 1819 - Art. 347 (2016); OECD Global Health Tax Revenue database and Euromonitor International.



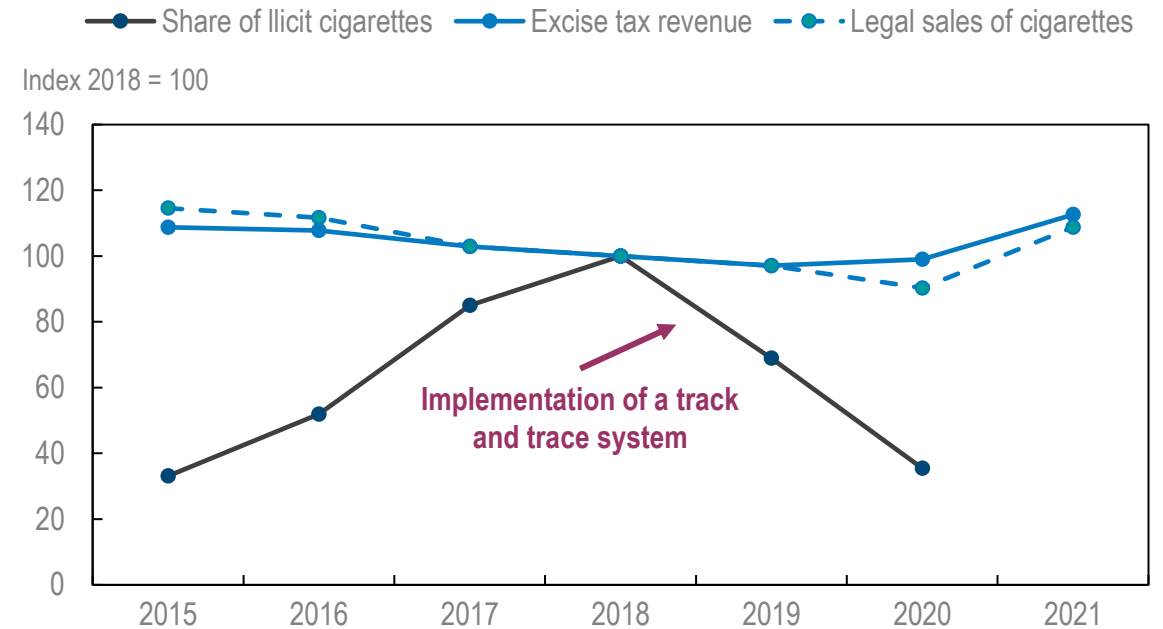
Concerns on revenue loss and illicit trade should not deter tobacco tax reform (II)

> Illicit trade in tobacco products calls for enhanced enforcement.

Illicit trade of cigarettes diverges across countries and is weakly correlated with price/ tax factors



Tracking and tracing cigarettes contributes to reducing illicit trade penetration (Chile)



Source: Drope, Rodriguez-Iglesias, Stoklosa, and Szklo, 2022; Paraje, Pruzzo, and Muñoz, 2023; PROESA-Universidad, 2023; Szklo AS, Drope J, 2024, for independent estimates on illicit trade; Euromonitor international for data on average price of legal cigarettes.

Note: Estimates on the illicit trade penetration are missing for 2021.
Source: [Paraje, Pruzzo, and Muñoz, 2023a](#) and [Paraje, Pruzzo, and Muñoz, 2023b](#).



The tobacco market responds strategically to tobacco tax reform (or the absence of it)

The tobacco market is continuously changing, and so tobacco tax reform should be dynamic and not static.



Tobacco companies respond strategically to tobacco tax increases to maximize their profits.

- > A tobacco tax reform aims at reducing the demand for tobacco products, which would have a negative impact on the profits of tobacco companies.
- > In response, tobacco companies adjust their behavior to minimize the impact, and therefore the effectiveness, of the tobacco tax reform.



The literature has identified multiple marketing strategies that tobacco companies implement according to market circumstances.

- > Strategic adjustments of prices of tobacco products (under- or over-pass through of the tax).
- > Price-related promotions.
- > Introduction of new brands targeted at particular niches of the market.
- > Changing product attributes or production processes.

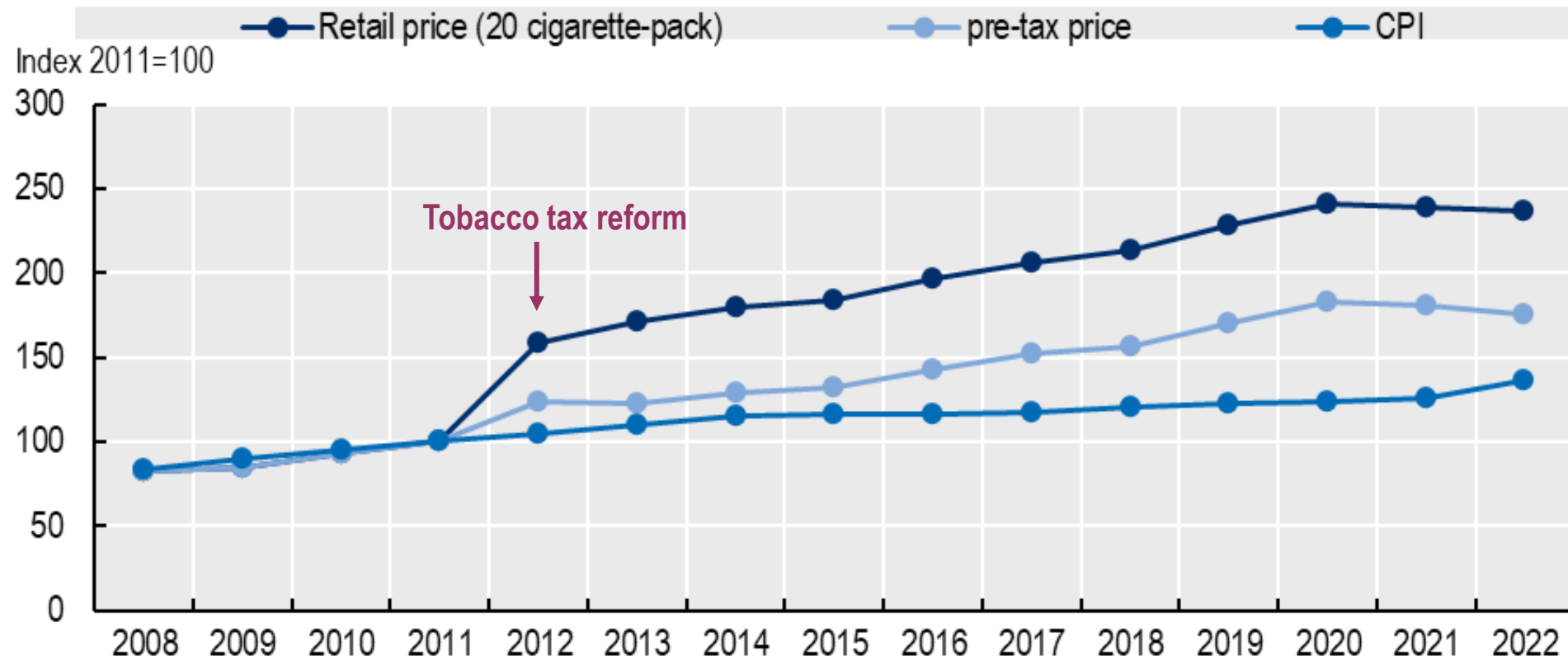


Country examples of industry pricing strategies (I)

Costa Rica: Overshifting strategy

- > The tobacco industry used the 2012 tobacco tax reform to sustainedly increase cigarette pre-tax prices above inflation.

Evolution of cigarette retail and pre-tax prices compared to inflation



Note: The average aggregate price used in this graph (retail price) is computed from Euromonitor International data, dividing cigarette sale values by cigarette sale volumes.

Source: Own computations using Euromonitor International data and World Development Indicators database.

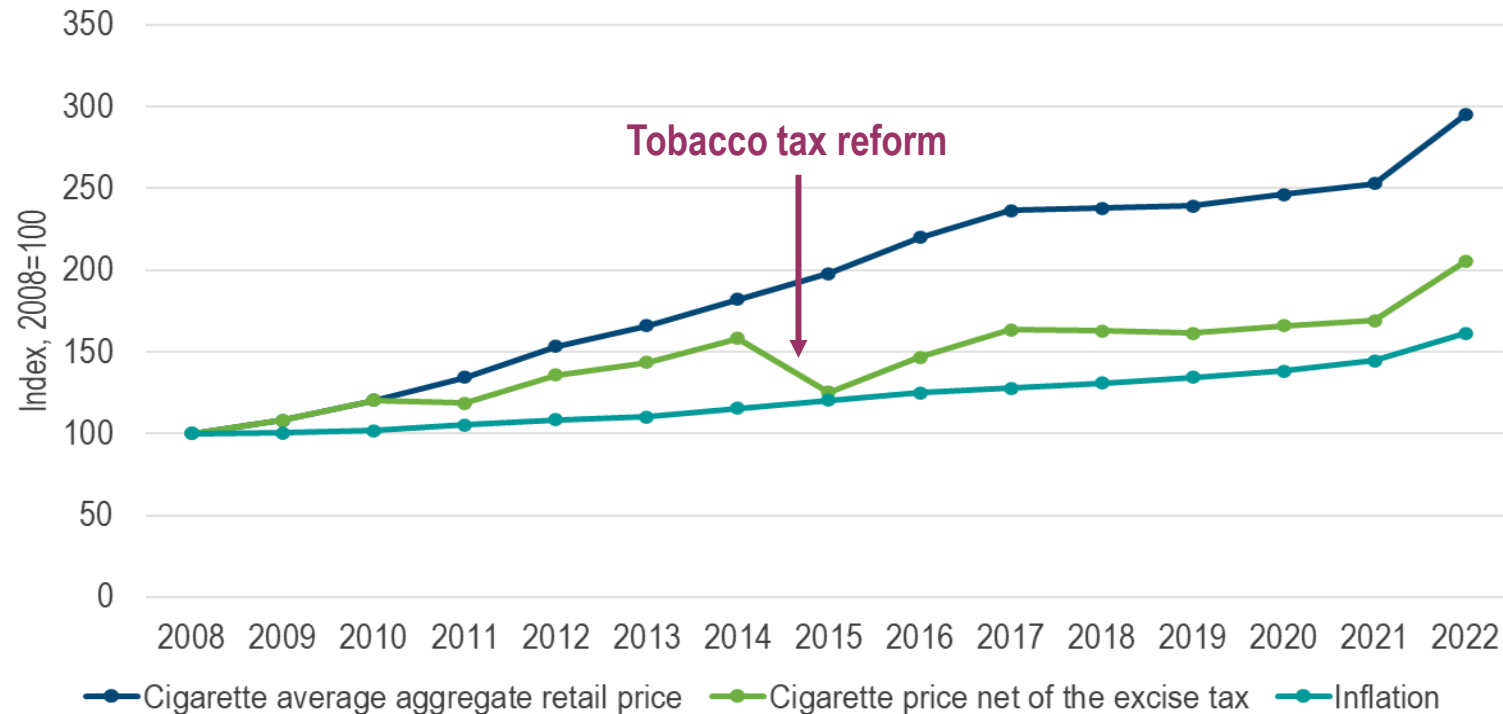


Country examples of industry pricing strategies (II)

Chile: Price smoothing

- > The tobacco industry partially absorbed the 2014 tax increase, and then gradually increased the prices net of excise tax above inflation.
- > This strategy might have mitigated behavioural responses from consumers.

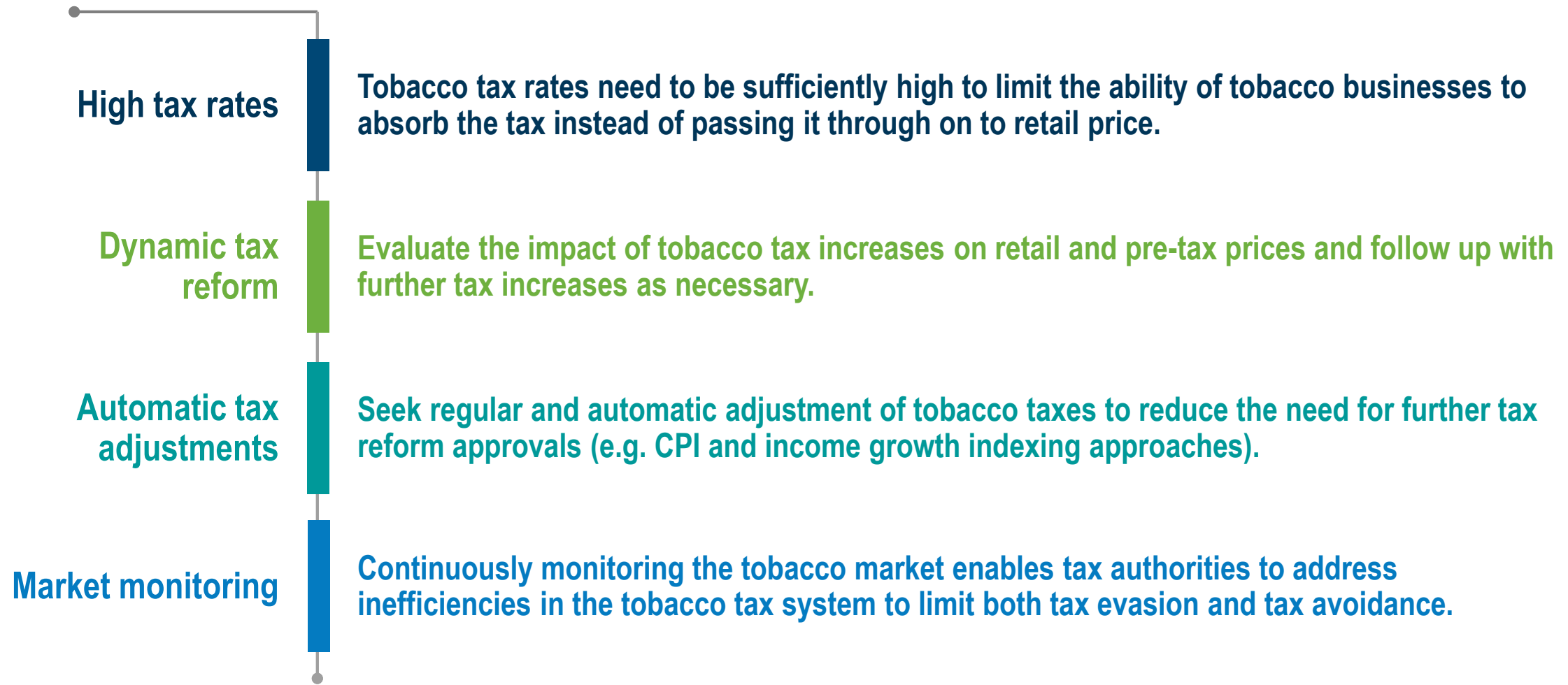
Evolution of cigarette retail and pre-excise prices compared to inflation



Note: The average aggregate price is computed from Euromonitor International data, dividing cigarette sale values by cigarette sale volumes.
Source: Own computations using Euromonitor International data and World Development Indicators database.



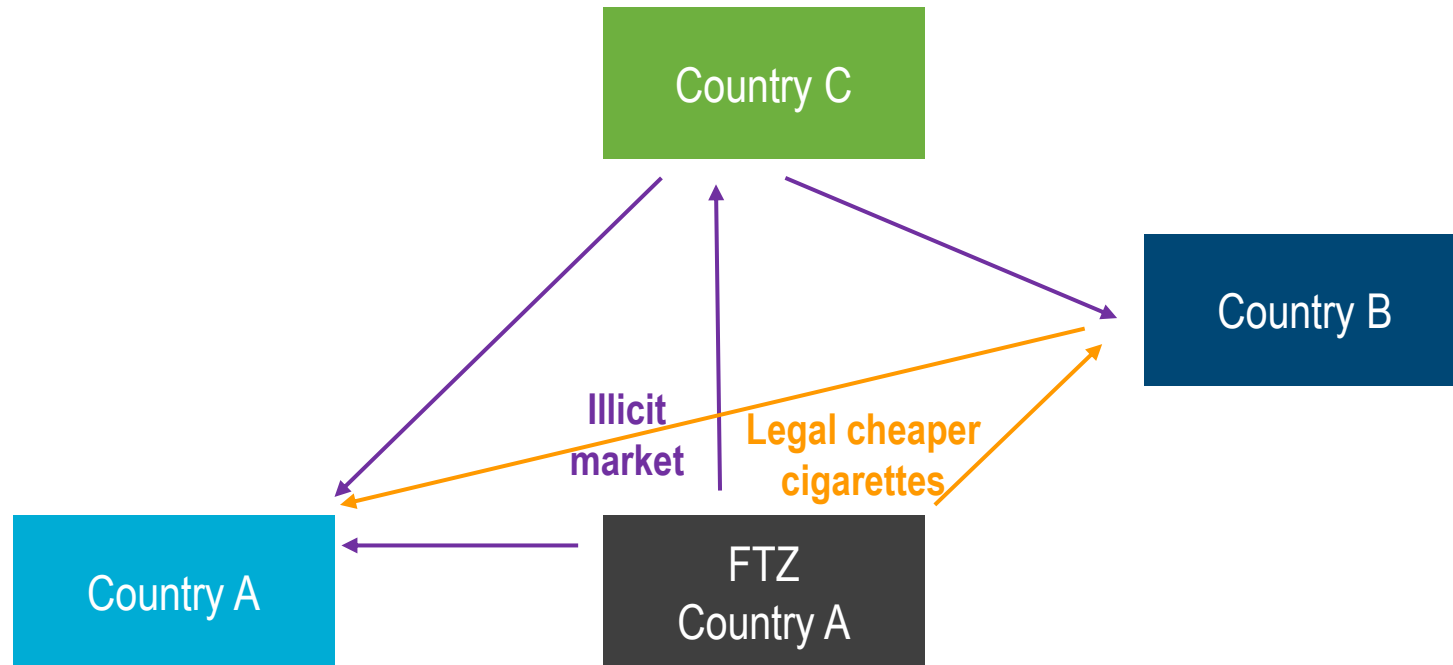
Industry strategic responses to tobacco taxes call for ambitious policy measures





Countries should collectively tackle the cross-border impact of weak tobacco control

Example of cigarette manufacturing companies in a Free Trade Zone (FTZ)



- Generous tax incentives → higher profitability, lower prices
- Regulation loopholes, lower enforcement → larger illicit trade opportunities

Free Trade Zone policies in Country A undermine the effectiveness of tobacco excise taxes in Countries A, B and C



Several tools are available for countries to cooperate globally on tobacco-related issues

- > **There is a lack of understanding of how tobacco multinationals operate globally.**
 - > Most of the information available is country-specific and significant gaps remain regarding the location of profits and cross-border pricing strategies.
 - > Individual governments lack the capacity and resources to comprehensively analyse the behaviour of tobacco multinationals.

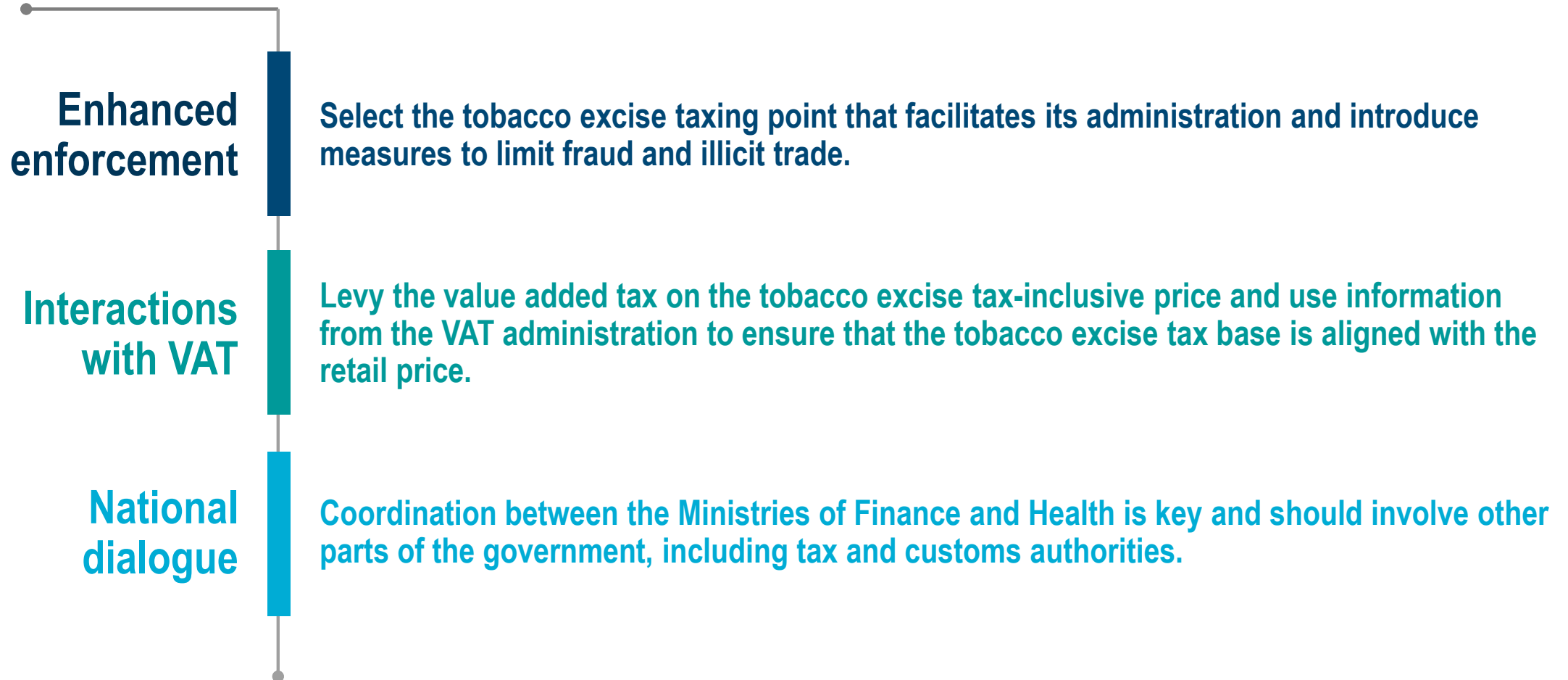
- > **Understanding how tobacco multinationals operate globally could contribute to improve the effectiveness of tobacco tax policies.**

- > **Mechanisms in place** for international cooperation on tobacco control:
 - > WHO Framework Convention on Tobacco Control (183 Parties, including 29 in LAC).
 - > WHO Protocol to Eliminate Illicit Trade in Tobacco Products (69 Parties, including 7 in LAC).

- > International tobacco tax cooperation could be **further strengthened by:**
 - > **Exchange of tobacco-related information** built on the experience that countries have in sharing income tax-related information (e.g. AEOI).
 - > **LAC Regional Tax Cooperation Platform.**
 - > **Compatible track and trace systems across countries.**



Additional recommendations to further strengthen the effectiveness of tobacco taxes



THANK YOU

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