

Illicit trade in tobacco products

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national treasury

Department:
National Treasury
REPUBLIC OF SOUTH AFRICA

The need to reduce tobacco consumption is clear

- According to the WHO FCTC, scientific evidence has unequivocally established that tobacco consumption and exposure to tobacco smoke cause death, disease and disability
- The WHO states that tobacco kills nearly 6 million people each year. More than five million of those deaths are the result of direct tobacco use while more than 600 000 are the result of non-smokers being exposed to second-hand smoke
- In order to deal with the negative consequences related to tobacco consumption, the Government has over the past decade introduced various policy measures (regulatory, taxation and expenditure)
- These measure range from banning tobacco advertising, restricting smoking in public places and increasing the targeted tax incidence for tobacco products

Excise duties are a recommended measure to curb use

- South Africa's tax regime (excise) for tobacco products is based on international benchmarks
- Rates are adjusted on an annual basis to account for domestic price movements and to maintain the benchmarked targeted tax incidence,
- Globally there is pressure from the health fraternity to increase the tax burden on tobacco products to account for the full negative external cost associated with tobacco consumption,
- WHO proposes that countries set their tobacco tax incidence equal to at least 70% of the retail price of tobacco products.

- An increase in illicit trade in tobacco products not only impacts on the fiscus (excise tax revenue forgone), but also hampers Government's regulatory mandate as well as national public health policies.

Excise duties follow a targeted tax incidence approach

- SA uses a targeted tax incidence approach which came into effect in 1994/95
- An initial tax incidence (excise tax plus VAT) was set at 50% of the retail selling price (RSP) of the most popular brand in each tobacco product category
- In Budget 2004, the tax burden benchmark increased to 52%
- In Budget 2015, shifted the focus on excise tax burden (i.e. removed the VAT component). As a result the current excise tax burden is set at 40%
- Excise taxes are adjusted annually to maintain the targeted tax incidence
- Real excise duties increased fivefold for a pack of 20 cigarettes between the period 1994/95 to 2014/15

The current excise duty per pack of 20 cigarettes is R15.20

Product	Cigarettes (per pack 20)	Cigarette tobacco (50g)	Pipe tobacco (25g)	Cigars (23g)
1999/00	R 2.45	R 2.29	R 0.62	R 7.53
2000/01	R 2.83	R 3.21	R 0.97	R 13.11
2001/02	R 3.17	R 3.58	R 1.17	R 15.28
2002/03	R 3.51	R 5.15	R 1.31	R 17.63
2003/04	R 3.89	R 6.22	R 1.46	R 24.52
2004/05	R 4.53	R 6.95	R 1.71	R 28.36
2005/06	R 5.05	R 7.47	R 1.91	R 32.59
2006/07	R 5.56	R 7.82	R 2.07	R 34.16
2007/08	R 6.16	R 8.24	R 2.18	R 37.73
2008/09	R 6.82	R 8.67	R 2.30	R 39.72
2009/10	R 7.70	R 9.15	R 2.50	R 44.88
2010/11	R 8.94	R 9.73	R 2.70	R 47.66
2011/12	R 9.74	R 10.53	R 2.98	R 50.52
2012/13	R 10.32	R 11.05	R 3.22	R 53.05
2013/14	R 10.92	R 12.16	R 3.54	R 56.76
2014/15	R 11.60	R 13.03	R 3.63	R 61.87
2015/16	R 12.42	R 13.94	R 3.89	R 64.96
2016/17	R 13.24	R 14.88	R 4.16	R 69.28
2017/18	R 14.30	R 16.07	R 4.56	R 75.86
2018/19	R 15.20	R 17.44	R 4.94	R 82.31

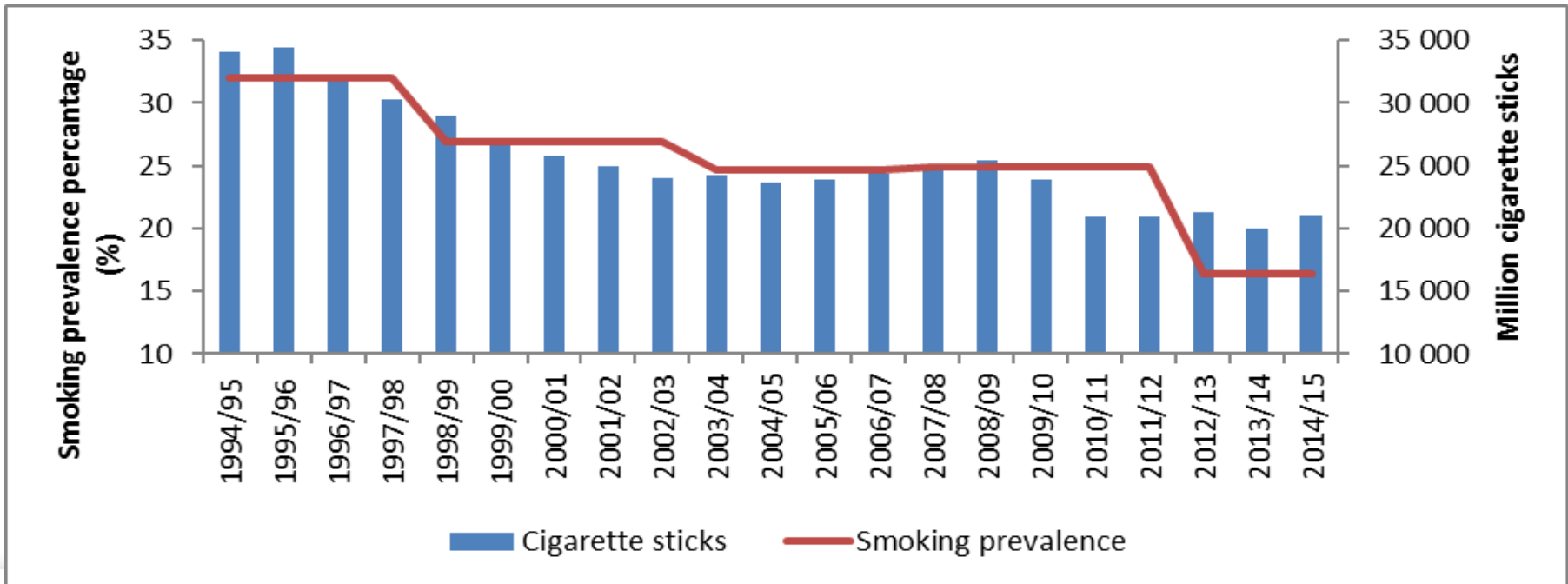
Alongside a variety of non-tax interventions

- Meaningful tobacco regulations really started with the Tobacco Products Control Act of 1993,
- Government implemented complementary non-tax policy interventions:

Regulation	Description
Tobacco Products Control Act, 1993	<ul style="list-style-type: none"> • Health hazard warnings and contents on advertisements and packages • Restrictions on vending machines • Prohibition of sales to people below age 16
Regulations, 1994	<ul style="list-style-type: none"> • Specifications on health warning and labelling requirements on packages
Tobacco Products Control Amendment Act, 1999	<ul style="list-style-type: none"> • Prohibition of smoking in public places except in designated areas • Bans on tobacco advertising and sponsorships • Bans on free distribution of tobacco products • Maximum content levels in cigarettes
Tobacco Products Control Amendment Act, 2007	<ul style="list-style-type: none"> • Bans smoking in selected outdoor areas. • Product regulation of imported and exported tobacco products • Standards for manufacturing and export of tobacco products
Tobacco Products Control Amendment Act, 2008	<ul style="list-style-type: none"> • Increase in age of sale from 16 to 18 • Bans on one-to-one advertising • Bans on tobacco-like toys • Bans on tobacco sales at health and educational establishments • Tighter bans on free distribution • Tighter standards on: <ul style="list-style-type: none"> – Packaging and labelling with pictorial health warnings – Point of sales and display

Smoking prevalence has been continually decreasing

- Smoking prevalence figures from South African National Health and Nutrition Examination Survey (SANHANES-1) suggests that there has been a steep drop in smoking prevalence numbers since implementation of the current excise regime in 1994.
- The prevalence rate was last estimated at 16.4%



Estimates of illicit tobacco vary, but generally high

- Illicit tobacco has a negative effect on tobacco tax revenue
- An increase in illicit trade in tobacco products not only impacts on the fiscus (excise tax revenue forgone), but also hampers Government's regulatory mandate as well as national public health policies.
- Abundance of cheap cigarettes undermines our health policy
- Various estimates of extent of illicit trade in tobacco, and will vary over time as enforcement and general business conditions improve or worsen

	UCT – Corne van Walbeek	Stellenbosch – Craig Lemboe	Evan Blecher (Cancer Society)	TNS Global
Model	Price and income (GDP) sensitivity: legal consumption vs. total consumption	Gap method: legal market + illicit = total market	Gap method: legal market + illicit = total market	Retail level survey: purchase events
Data	Treasury & Stats SA	Treasury & AMPS	Treasury, AMPS, DHS, NIDS & SANHANES	Treasury, AC Nielsen & Survey data
Period	1999 – 2013	2001 – 2011	1997 – 2012	2007 – 2012
Estimate	4 – 17.9 % 20.4 % (2011/12)	≥ 20 % Average 24 %	8 – 12 % gap method 17 % (2011)	11 - 30 %

Government involved in international measures to counter illicit trade

- SA signed to be a Party to the Convention in 2005 and has since begun to align its Tobacco Control legislation.
- Article 15 of the Convention provides for the elimination of all forms of illicit trade in tobacco products, including smuggling and illicit manufacturing
- Illicit trade increases the accessibility and affordability of tobacco products, fuelling the tobacco epidemic and undermining tobacco control policies.
- Also causes substantial losses in government revenues, and at the same time contributes to the funding of transnational criminal activities (WHO,2013)
- The WHO FCTC Protocol to Eliminate Illicit Trade in Tobacco Products is the first protocol under the Convention (was adopted in November 2012)
- The Protocol requires of Parties to adopt and implement effective measures to control or regulate the supply chain to prevent, deter, detect, investigate and prosecute illicit trade
- NDoH is leading government process to ratify the Protocol

And further measures are being implemented and explored

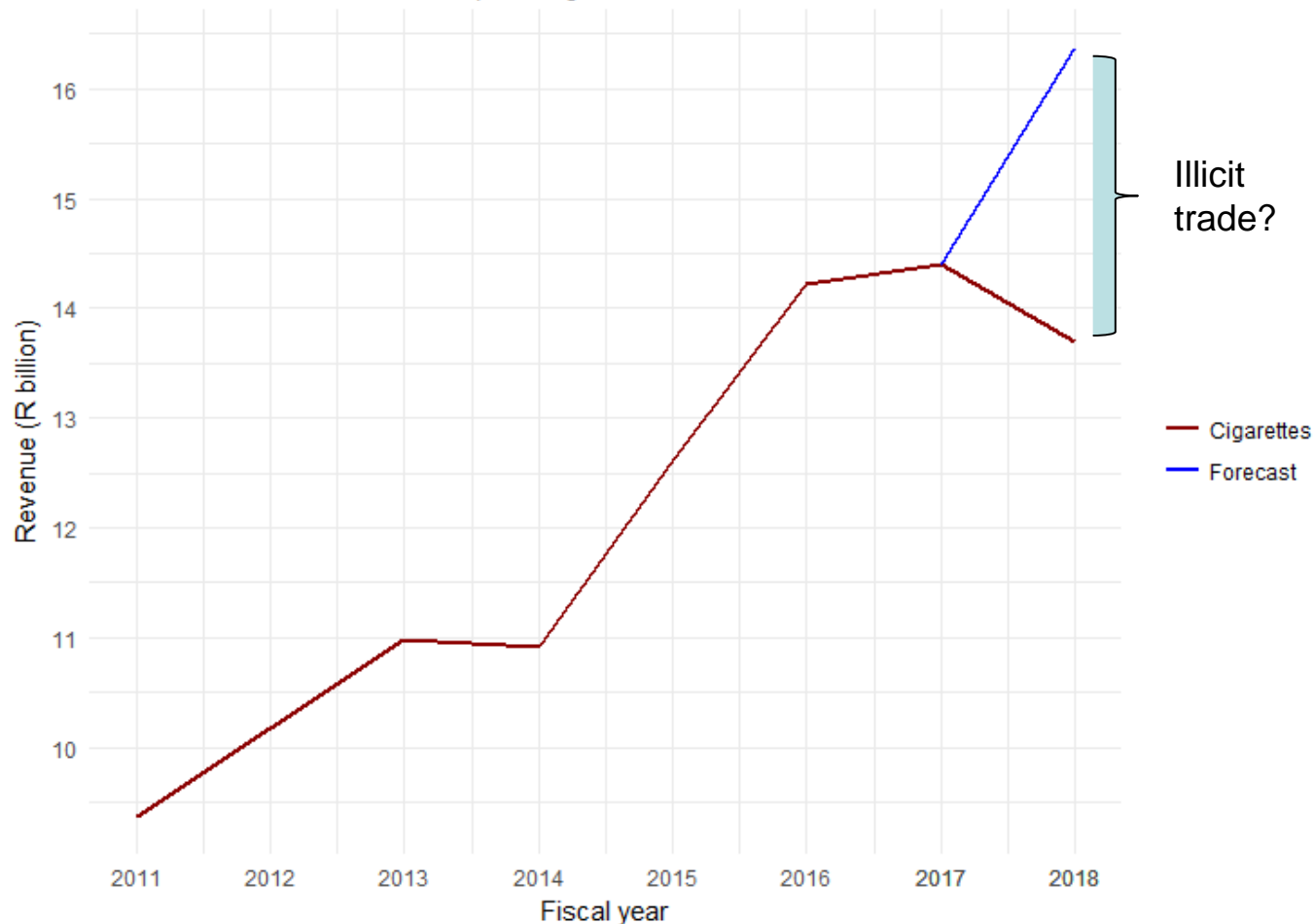
- Due to increased awareness of illicit tobacco trade, the National Treasury facilitated a workshop in 2013 to deliberate on the extent of illicit trade
- In 2017 Budget, it was announced that amendments will be considered for the provisions in the Tax Administration Laws Amendment Act (2016) for the marking, tracking and tracing of tobacco products
- The 2018 Budget announced that
 - “*The National Treasury and the Department of Health will explore additional measures to reduce consumption of tobacco products, including a minimum price and stronger enforcement.*”
- Should any retailer be selling a pack of cigarettes that is less than the R15.20 excise duty?
 - May be easier to enforce and clearer for the public to identify illicit products

Last two years have been particularly worrying from a revenue perspective

- Budget 2017 estimated revenue from domestic excise on cigarettes was R15.04 billion
- Outcome was R11.07 billion (26% decrease)
- Partly due to large domestic manufacturer leaving SA
- But still **down close to R3 billion** when including imported cigarettes
- Appears to be due to increases in illicit trade (unless consumption has collapsed – note alcohol excise outperformed over same period)

Tax revenue from excise duties on cigarettes and cigarette tobacco

Revenues from both domestic and imported cigarettes



Illicit tobacco closely linked to serious allegations made in media, needs to be investigated by Commission of Inquiry

- If revenues are falling due to lower consumption, that is a good thing (but no evidence that this is true and seems unlikely over such a short period)
- Does appear to be due to increases in illicit tobacco (which is a view echoed by some in the tobacco industry)
- NT does not believe a more accommodative excise policy is warranted or will assist in reducing illicit tobacco
- Is the increase in illicit tobacco trade due to declining resources, particularly a lack of intelligence capacity, at SARS?
- There may need to be greater co-operation with other authorities (SAPS, NPA) to target the problem
- There have been numerous media reports and books written on these issues and need to find out if there is any substance to these allegations
 - The Commission of Inquiry should investigate these matters
 - Industry itself face serious allegations, which may have ultimately contributed to undermining enforcement

THANK YOU



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Annex: Tobacco Tax Review

Budget 2016 announced that a review of the current tobacco tax regime will be undertaken and the National Treasury is currently busy with this process.

Focus will be on

- Experience thus far,
- Other policy considerations such as:
 - √ The scope for potentially increasing tobacco taxes,
 - √ Possibility of a uniform tax across all categories,
 - √ Price points used for adjustments,
 - √ The role of minimum prices,
 - √ Tax treatment of non-combustible tobacco and tobacco substitutes,
 - √ The most desirable package of interventions needed in order to decrease tobacco use,
 - √ Other New developments,