

Opinion: Seeing through the cigarette tax smokescreen

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The high taxes on tobacco are counterproductive in decreasing smoking. It only benefits the illegal cigarette trade—and its political masters.

Selling addictive substances as a commercial activity is always a winner. Demand is locked in, even if prices rise. Alcohol, narcotics, money, sex, gambling, and, of course, nicotine are where money grows on trees for suppliers.

Addictions, however, become particularly harmful where they interfere with a person's ability to pursue their normal daily activities—for instance, where family relationships, employment and social interactions are harmed. Physical harm can also result from addictive practices including smoking, the use of narcotics and [excessive alcohol consumption](#). In the case of narcotics and alcohol abuse, harm can extend to non-users through acts of violence and direct and indirectly related criminality.

Social controls have consequently been introduced for very dangerous substances where there are clear risks to individuals and society—many with only limited success. Over time these controls have included blanket prohibitions, the criminalization of the sale and distribution of certain products, stringent licensing conditions, the supervision of transactions and so called "sin" taxes or excise taxes.

Such approaches have, however, been notoriously unsuccessful in controlling trade, distribution or consumption, and have typically succeeded only in driving these activities underground. Due to their very nature and the sustained demand for addictive substances, poorly designed [control measures](#) merely lead to the growth of well-funded criminal syndicates some in collaboration with corrupt elements within the state.

While many [addictive substances](#) are extremely harmful, at a social level smoking falls into a category of harm that is sufficiently mild to avoid more stringent and weighty control, yet sufficiently harmful to attract a degree of regulation.

Any form of product control where a natural and sustained market exists, however, brings with it opportunities for corruption and patronage, with the risk that [public health measures](#) will be rendered futile.

If the price is right

A largely successful public interest lobby has existed in South Africa to reduce demand through the implementation of a consumption tax on cigarettes, in the form of a 40% ad valorem tax on top of VAT. Consequently, over 50% of the price of a legally traded packet of cigarettes goes to SARS. What might have been more effective is a specific tax with a fixed Rand value, rather than using the percentage levy.

This means that legitimate manufacturers can, therefore, offset any drop in demand due to the ad valorem tax through price manipulation. Tobacco brands targeting price-sensitive (low income) segments of the market are discounted, with [high prices](#) reserved for the less price sensitive (high-income) smokers.

Manufacturer strategies aside, smokers remain impervious to price fluctuations—precisely because the product is addictive.

While there does appear to be some correlation between the effects on demand and tax increases on cigarettes in South Africa, there is, however, no studies to show the impact that non-financial penalties such as legislation around target marketing and smoking in [public places](#), have had.

A flourishing illicit trade

Further confounding the picture is the growth of the illicit trade in cigarettes. Illegal manufacturers simply do not charge the excise tax, giving them a significant price advantage over legal manufacturers. Not surprisingly, the higher the prevailing tax, the greater their price advantage.

Within South Africa there is also an apparent linkage between these illicit actors and parts of the political establishment with the result that investigations into illicit markets by, among others, the South African Revenue Services (SARS) appear to have been suppressed.

The question now arises whether the calls for further [public health](#) interventions by government to control smoking have their origins in a legitimate concern for public health or are driven by players in the illicit market working through their political principals.

The apparent demand-related effects of the various anti-smoking measures are also unclear as no data is available on the illicit trade. It is entirely plausible, therefore, that when the illicit trade is considered, overall demand for tobacco products is increasing and not decreasing.

During COVID-19, the prohibition on the trade of cigarettes appeared to have no impact on demand whatsoever, with illegal trade filling the void left by the enforced withdrawal from the market of legal manufacturers. The fiscus consequently lost millions in tax revenue, with zero public health gains.

Political patronage

South Africa was the only country in the world that regarded this prohibition as an appropriate response to the pandemic. It appeared to many that the move in fact had very little to do with COVID-19, and a lot to do with political patronage in the illicit market.

The emergence of an illicit cigarette market with established links with government officials is, however, a predictable outcome of the very high excise taxes and VAT, coupled with an unwavering demand for an addictive substance.

Exorbitant tax levels eventually become self-defeating, as illicit actors derive significant financial advantage from learning how to beat the system—including through corrupt relationships with the state.

The more punitive the tax, the greater the incentive to circumvent it. The greater the incentive, the more likely that corruptible state officials will be drawn into the picture.

As a result, the public health imperative becomes a smokescreen (pun intended) for the true motive—which is to divert demand away from taxed cigarettes to untaxed cigarettes, despite serious adverse implications for both public health and government revenue.

A new model to manage tobacco is needed

In conclusion, a more coherent model for regulating the tobacco industry is clearly called for. One that speaks to inter-related objectives—such as tax revenue maximization and public health benefits.

First, taxes could be reduced to a level that would allow for the maximization of tax revenue without creating incentives for a persistent illicit market. A more moderate excise tax may yield better results in the reduction of smoking by being set high enough to disincentivise smoking in lower income groups and children, while generating an acceptable tax revenue but undermining what is an entrenched illicit market.

Second, public health interventions should be diversified at the same time as being acknowledged for their inherent limitations. This includes

the regulation of marketing, smoking in public spaces and measures to avoid the adoption of smoking by children.

However, ultimately, it is arguable that in relation to smoking and the consumption of tobacco products, non-tax related measures are more likely to prove successful than excise levies in the achievement of public health objectives.

Provided by Wits University

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