



Removing incongruities in tax policy on tobacco sector

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By *Dr. Ahsan H. Mansur*

Bangladesh's existing tax structure is significantly boosting the consumption of cheap low segment cigarettes and bidis at the expense of upper segments of cigarettes, thus causing a large-scale revenue loss for the National Board of Revenue (NBR).

The lower tax rates and the consequent lower prices have led to a rapid growth in the consumption of low segment cigarettes and bidis in volume terms, undermining the main objective of tobacco-control policy.

Lower tax rate has allowed the low segment cigarettes to raise their market share from 36 per cent to 63 per cent in the last six years, though its current share in tobacco revenue now hovers between 20 per cent and 22 per cent..

Volume of low segment of cigarettes, which is taxed at the rate of only 56.9 per cent of final retail price, expanded primarily at the expense of medium segment cigarettes bearing 76 per cent tax.

In the combined smoking industry of bidis and cigarettes, bidis currently account for 47 per cent of the market share, but only 2.0 per cent of revenue is mobilised from this sub-standard segment of the smoking industry.

Market shares of high and premium segments of cigarettes that are taxed at a much higher rate declined from 18.1 per cent to 11 per cent and from 6.2 per cent to 4.8 per cent, respectively, during the same period since the fiscal year (FY) 2007-08.

Accordingly, the government is getting much lower amount of revenue from each unit of cigarettes-bidis due to fall in consumption of higher-taxed and priced premium, high and medium segments of cigarettes against increased consumption of low segment cigarettes and bidis.

To up-trade the market to medium, high and premium segments and increase collection of revenue, the government has to increase the tax rate and price on the low segment of cigarettes and bidis.

The global standard for the price ratio between the most expensive and cheapest popular brands is 2:1, while in Bangladesh it is currently, at least, 6:1.

This must change and the only way to do this is to raise the price of low segments cigarettes and bidis by, at least, 10-15 per cent more than the annual increase in per capita income.

Such an strategy would entail a minimum 25 per cent increase in price of cheaper tobacco and bidis annually over the next five years if we really intend to achieve the social objective of reducing tobacco consumption.

Compared to increase of people's income, the price of the high segment of cigarettes rose by 6.8 per cent during the last six years while the corresponding increase was only 2.9 per cent in the case of low segment cigarettes. That is not enough.

In this context, many people may suggest reduction of tax on the low segment cigarettes considering that those are consumed by the poor. This may also be done in Bangladesh in the case of taxation on their income and others, but such a policy cannot be taken on the issue like tobacco; that will harm them.

We have to raise the tax rate on, and price of bidis and low segment cigarettes. And there is little scope to increase tax rate on the upper segments, because those are already being taxed at very high rates. Their prices should be kept at a tolerable level to prevent the smuggled-in cigarettes taking over the market.

Bidis are taxed at much lower rates than cigarettes, despite its 47 per cent market share in volume terms and accounting for only 2.0-3.0 per cent of revenue from tobacco products. This is because bidis are subject to a much lower rate of tax and the tax is imposed on tariff values set by the government, which are approximately half their actual retail prices.

It is simply irrational to keep the tax rate on bidis at an artificially lower level. This will widen the scope for the poor people to smoke more and suffer from the ill-effects of smoking.

In fact, there is no need for bidis in today's Bangladesh. Bidis is the worst form of legally permitted smoking item. It is outdated and old-fashioned.

Given Bangladesh's current per capita income of \$1314, even the farmers now can easily afford to smoke cigarettes.

In Bangladesh, the cigarettes, especially those of popular brands, are sold at the lowest price compared with those of other countries. Accordingly, it is better to introduce a uniform tax structure for all segments of cigarettes and bidis, and discard the practice about fixation of the ceiling price of cigarettes by the NBR.

The higher is the price, the more tax the NBR will get. Why should there be any price ceiling then?

The target for the NBR-portion of the revenue in the next budget will be very ambitious, because the government will need resources to implement its economic, social and political

vision.

For a sustained growth of revenue, the government has to implement reforms in the income tax and value added tax (VAT), and modernise the taxation administration.

It is a well-established fact that increased tax revenue will have to come primarily from income tax and VAT in the medium term but with a lag of one to two years, even if we implement the much-needed reforms today.

Taxation of tobacco through rationalisation of the tax structure and liberalisation of the pricing policy can play a very important role in achieving the revenue target for FY16 budget.

The immediate additional revenue gain could be up to Tk. 35-Tk. 40 billion.

The government needs to look seriously into the matter and not buckle under pressures from vested interest groups.