

# UNDERMINING GOVERNMENT TAX POLICIES



## Common legal strategies employed by the tobacco industry in response to tobacco tax increases

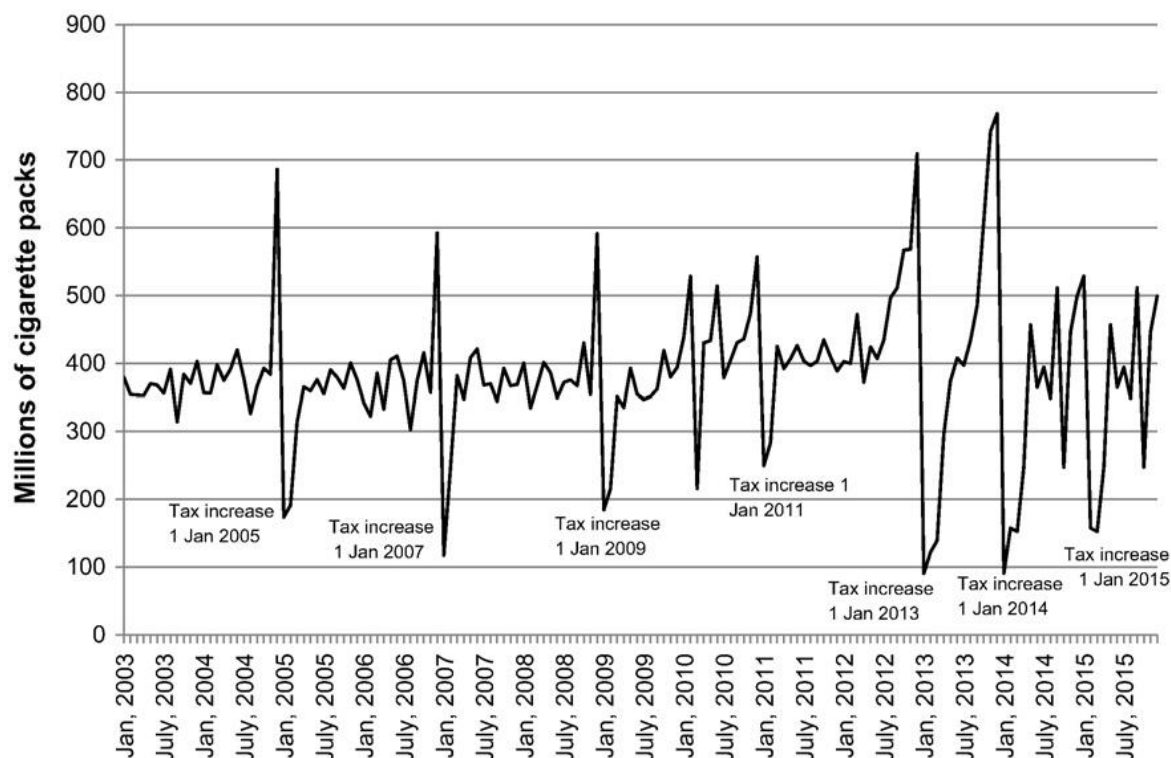
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Effective tobacco tax increases reduce tobacco consumption, threatening the profitability of the tobacco industry. In response, the tobacco industry employs strategies to negate or minimize

the full effects of tobacco tax increases. By interacting with various government agencies and non-governmental organizations we identified 7 of these strategies:

### 7 STRATEGIES

1. **Stockpiling** (forestalling/front-loading) is over-supplying the market before a tax increase to pay the pre-tax-increase rate.
2. The tobacco industry can **change product attributes** (e.g., weight, length) or production processes if different tobacco products have different tax increases.
3. **Lowering producer prices** on some or all products in an ad valorem tax regime reduces tax payments.
4. **Over-shifting** a tax increase raises retail prices more than the tax increase. Higher profit margins compensate the industry for the reduction in sales due to higher tax.
5. **Under-shifting** tax increases is usually a temporary attempt to preserve sales as the industry absorbs a part of the tax increase, usually on low price brands.
6. **Strategic timing** of a price increase allows the customers to adjust gradually to higher prices, which may result in an overall smaller decrease in tobacco demand compared to increasing prices in one step.
7. **Price discrimination and/or price-related promotions** minimize the loss of price-sensitive customers after a price increase by offering discounts, retailer rebates, or adding value (e.g. gifts) to the purchase.

**Stockpiling in the Philippines 2003 – 2015: Volumes of cigarette removals**

Source: Department of Finance - Fiscal Policy and Planning Office (DOF - FPPO) and the Bureau of Internal Revenue (BIR) of the Republic of the Philippines, 2016.

## POLICY LESSONS

- Many of the tobacco industry's responses to tobacco tax increases are predictable, since they are being employed systematically across countries.
- Governments have the power to regulate the industry and can use the Article 6 Guidelines of World Health Organization's Framework Convention on Tobacco Control to prevent these tax avoidance practices.
- An effective tax administration requires monitoring and analysing the industry behaviour so that authorities can respond quickly and effectively. This will enhance tax collection and improve public health by increasing the effectiveness of tobacco excise taxes.

### Link to full research paper:

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