

Smokefree Coalition submission to the Finance and Expenditure Committee on the Budget Policy Statement 2007

1. BACKGROUND

The Smokefree Coalition (SFC) is a charitable trust, originally established in 1995. It exists to advocate for more effective tobacco control interventions from the government and other agencies.

Its vision is of a smokefree New Zealand but within a legal framework where smoking remains a legal activity (but within appropriately defined settings).

There is strong scientific evidence that reducing the prevalence of smoking among the population will have beneficial social and economic effects for the health of individuals and for the community as a whole.¹

This submission has been circulated to a wide network of organisations with an interest in public health and consumer affairs and is endorsed by: The Asthma and Respiratory Foundation, The Quit Group, The New Zealand Stroke Foundation, The New Zealand Heart Foundation, The New Zealand Drug Foundation and the Consumers Institute. It is also personally endorsed by Dr Nick Wilson of the Wellington Medical School, University of Otago.

Recommendation

We are here today to submit that, in its consideration of the Budget Policy Statement 2007, the Finance and Expenditure Committee should recommend to the government that:

- 1 there should be an immediate substantial increase in the taxation of tobacco, and,***
- 2 there should be regular and predictable annual increases in tobacco taxation which are significantly greater than any rise in the prevailing consumer price index (CPI), and,***
- 3 there should be an immediate increase in the taxation on loose tobacco (roll your owns) to remove any price advantage over tailor made cigarettes (per cigarette), and,***

¹ Collins DJ, Lapsley HM. Counting the costs of tobacco and the benefits of reducing smoking prevalence in NSW. NSW: McQuarrie University and University of Queensland.

4 a significant proportion of the taxation revenue raised from this source should be used to fund improvements in tobacco control (so that the ethical basis for increasing tobacco taxation is strengthened).

2. SUBMISSIONS

The problem

There is no doubt that smoking kills. It is one of the largest causes of preventable death (to say nothing of disease) in the world.

Tobacco use is the leading cause of preventable death in New Zealand, accounting for around 4300 to 4600 deaths per year.² Half of the people who smoke today will eventually be killed by tobacco if they continue to smoke long-term.³ Half of these people are likely to die in middle age.⁴ Second-hand smoke is estimated to cause around 350 deaths per year in New Zealand⁵ (though this figure may start to decline with the recent legislation).

To put this death burden into context – it means fourteen New Zealanders will die today, and every day, of smoking-related illness. In the time that it takes for this committee to hear evidence on the budget policy statement, at least one New Zealander will have died from a smoking-related illness.

The death burden has shifted little (if at all) in the twelve months since we first submitted to this committee. One reason for this can be attributed to the fact that smoking prevalence, while declining slightly, still remains at about one in four of the population.⁶

The solution

There is strong scientific evidence for price as a key economic tool to discourage smoking uptake by youth as well as acting as an incentive for people to quit smoking.⁷ In this regard we see the use of taxation as a

² Peto, R, Lopez, A, et al. (2000). *Mortality from Smoking in Developed Countries 1950 – 2000: Indirect estimates from national vital statistics*. New York: Oxford University Press.

³ World Health Organization. *Why is tobacco a public health priority?* Tobacco Free Initiative. Retrieved on 23 January 2006 from http://www.who.int/tobacco/health_priority/en/print.html.

⁴ Peto, R, Lopez, A, et al. (2000). *Mortality from Smoking in Developed Countries 1950 – 2000: Indirect estimates from national vital statistics*. New York: Oxford University Press.

⁵ Woodward A, Laugesen M (2001) How many deaths are caused by second-hand cigarette smoke? *Tobacco Control*. 10, 383-8.

⁶ Ministry of Health. (2006). *Tobacco Trends 2006: Monitoring tobacco use in New Zealand*. Wellington: Ministry of Health.

⁷ Guindon E, Perucic A, Boisclair D. (2003). *Higher Tobacco Prices and Taxes in South East Asia, An Effective Tool to Reduce Tobacco Use, Save Lives and Generate Revenue – HNP Discussion Paper*. Economics of Tobacco Control Paper no 11. The World Bank.

legitimate measure to increase the price of tobacco products and thereby reduce smoking rates.

The last increase in tax on tobacco products was in 2000. The tax increase raised the price of tobacco products by approximately 14 percent (one dollar per pack of 20 cigarettes). Tobacco companies added further price increases, resulting in an overall price increase of approximately 20 percent.⁸ However, over time, this increase has devalued. Consequently the real price of cigarettes remains unchanged from its 2000 base and, with the increase in real wages in that time, cigarettes have gradually become relatively more affordable.

Draft reports on research commissioned by the Smokefree Coalition and ASH into the effects of taxation on tobacco strongly suggests that year-on-year real incomes have increased since 2000 (see Appendix 1).

Coupled with this, the same draft reports show a real levelling off of revenue from tobacco taxes and excise from its peak in 2003 (see Appendix 2).

While this research has not yet been completed, in view of the speed with which this committee needs to make recommendations and the timetable for the Government's budgetary considerations, we felt it important to make the committee aware of even the preliminary findings which support the argument that tobacco has become relatively more affordable, even if one ignores the price advantage of loose tobacco when compared with tailor-made cigarettes.

It is not easy to tell from the Half Year Economic and Fiscal Update (accompanying the Budget Policy Statement) what the forecasts for revenue from tobacco taxes and excise will be. However, neither the Budget Policy Statement 2007 nor the Half Year Economic and Fiscal Update (December 2006) foreshadow any policy change in this area. We can only assume that any rates increase will be by the CPI as has been the case up until now.

There are three points to be made about this. First, a change is taking place in the source of tobacco revenues. With the decline in New Zealand-based cigarette production (from shifts to Australia) revenues have largely shifted away from excise to customs duty. Secondly, tobacco tax revenues appear to have levelled off no matter how it is measured. This is because there has been no real increase in tobacco tax rates, above inflation, since 2000. Finally consumption per head has continued to drop since 2001. A large decline occurred in 2003, though there has been some increase since that time. However it is fair to conclude that the consumption drop achieved in 2000 has eroded.⁹

⁸ Ministry of Health. Tobacco Tax – the New Zealand Experience. Wellington: Ministry of Health.

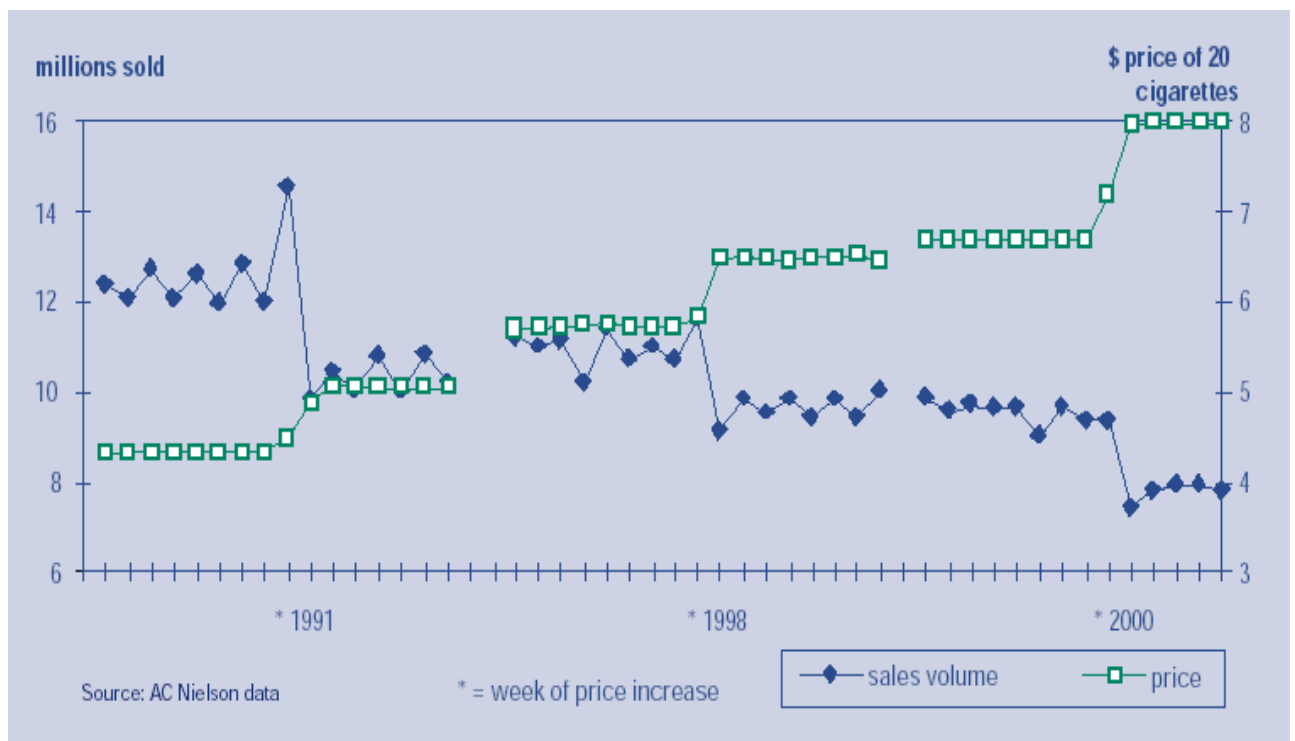
⁹ See *Tobacco Trends 2006*, Ministry of Health.

It has been the policy of successive Governments to press for a reduction in smoking prevalence. Tax increases are a legitimate tool in a comprehensive tobacco control strategy aimed at achieving this.

The World Bank concludes in a 1999 report that, on average, a price rise of 10 percent would be expected to reduce demand for tobacco products by about 4 percent in high income countries and about 8 percent in low and middle income countries. Also, that the impact would be significant among youth.¹⁰

New Zealand's experience is no different. A Ministry of Health document *Tobacco Tax – The New Zealand Experience* shows a clear relationship between price and consumption, where an increase in price shows a corresponding drop in sales.

Manufactured cigarette sales before and after the Budgets of 1991, 1998 and 2000 (using data from supermarket checkouts). From *Tobacco Tax – The New Zealand Experience*.



¹⁰ Guindon GE, Tobin S, Yach D (2001). *Trends and affordability of cigarette prices: ample room for tax increases and related health gains*. World Health Organization.

The arguments around tobacco tax increases

As a counter to increasing tax on tobacco, it is often argued that current taxation meets the immediate health-related costs for those who smoke. This argument ignores the full costs of tobacco and the benefits of reducing smoking prevalence. In 1997, economist Brian Easton estimated the annual tangible and intangible cost in 1990 of tobacco use in New Zealand to be \$22.5 billion.¹¹ Even the tangible costs alone, then at \$1220 million were considerably more than the annual tobacco tax-take, which is now around \$900 million.

A study for the New South Wales government provides a useful insight to this issue.¹² New South Wales has a population of around 6.7 million people.

This report (among other things) concludes that:

- i. the total social costs of smoking in NSW in 1998/99 were about \$6.6 billion
- ii. of these costs 27.1% were tangible and 72.9% intangible (loss of life)
- iii. 45% were avoidable with appropriate public policy
- iv. individuals bore 58% of total tangible costs, business bore about 29%, and governments 13%. Individuals bear 100% of the intangible costs.

The economic gains from effective tobacco control interventions

The New South Wales report estimates the benefits from a five percent reduction in smoking prevalence over five years at a conservative figure of \$2.366 billion to a most plausible (not most favourable) figure of \$5.835 billion. (These figures are assumed as accruing over the whole of a twenty-year period).

Besides longer and better quality lives, tangible economic gains come from increased productivity, reduced absenteeism and an increased workforce with consequent increased tax revenue and incomes; and reduced health, fire, insurance and other costs.

The authors support the adoption of the conservative assumption for the purposes of policy discussion. This report is helpful to inform debate and can be used with confidence when making policy decisions.

¹¹ Easton B (1997). *The Social Costs of Tobacco Use and Alcohol Misuse*. Public Health Monograph. Wellington: Department of Public Health, Wellington School of Medicine.

¹² Collins DJ, Lapsley HM. Counting the costs of tobacco and the benefits of reducing smoking prevalence in NSW. NSW: McQuarrie University and University of Queensland.

Equalising Roll-Your-Own Cigarettes and Tailor Made Cigarette Tax

Table 1. “Comparison of taxation of tailor made cigarettes and roll-your-owns”¹³

	Ready-made cigarette	Roll-your-own cigarette
Weight of tobacco	0.8g	0.6g
Tax per cigarette	\$0.2794	\$0.20955
Total tax per 20 cigarettes	\$5.59	\$4.19

(The calculations in Table 1. are based on the 2006 taxation rates. The December CPI series has not been calculated in the numbers.)

What Table 1 shows is a real price advantage for roll-your-own cigarettes (the close alternative to tailor-made cigarettes). In order to discourage switching from tailor-made cigarettes to roll-your-owns, instead of quitting, the price advantage needs to be stopped. This holds true too for the person looking to initiate smoking.

It is our submission that the tax on roll-your-own tobacco needs to be increased immediately by \$1.40 per packet (in 2006 dollars increased by the December CPI series).

3. CONCLUSIONS

Evidence is emerging that the “gains” to public health made from the 2000 tax increases on tobacco have eroded. During the subsequent years real year-on-year incomes have increased while tobacco excise has levelled off.

Smoking prevalence among the population, while dropping marginally, is still around one in four according to published Ministry of Health reports. That is above the rates in many other countries (including Australia and some US states).

It is clear from Ministry of Health figures and other research¹⁴ that tobacco price increases reduce the incidence of smoking in the population.

It is therefore our position that this committee, to promote economic and health gains, should recommend to the Government that there be an immediate and substantial increase in taxation on tobacco products in this

¹³ “Smoking Times” Issue 83, June 2006, Action on Smoking and Health

¹⁴ Wilson N., Thomson G. *Tobacco tax as a health protecting policy: a brief review of the New Zealand evidence.* NZMJ, Vol.118, No 1213, 15 April 2005.

year's budget. In doing so the price advantage of loose tobacco (roll-your-owns) needs to be removed.

Further, it is our position that an index other than the CPI should be used to regularly increase the excise on tobacco products.

While preliminary research shows a strong case for a "tied tax" for tobacco control from tobacco revenue, it is our position this year that a significant proportion of the increased tax take should be directed to tobacco control initiatives such as health promotion, smoking cessation, enforcement of current smokefree laws and tobacco control research.

In the case where the Committee feels unable to go that far (though we can see no good reason why that would be the case) this submission will serve as notice that this matter is a key issue for the tobacco control community. The price of tobacco products must become, and remain, relatively expensive thus discouraging new entrants and encouraging smokers to quit.

Thank you for your attention to this issue.

APPENDIX 1

Extract on 'Income Indexation' from draft report on Tobacco Taxation

A.1.4 Income trends

Tobacco excise rates are adjusted regularly for consumer price inflation, so as not to fall in 'real' terms. By and large the retail price of cigarettes (as measured by the Statistics NZ Cigarettes and Tobacco CPI sub-group index) appears to have increased in recent years by at least as much as the increases in the excise tax, and usually more. That is, the 'indexation' of tobacco excises has been accompanied by increases in cigarette retail prices at least equal to increases in consumer prices.

Over the long term, however, average incomes have increased in real terms, making cigarettes more 'affordable', as measured for example by the number of minutes of work at average wages required to purchase one packet of cigarettes (*Tobacco Statistics 2000*).

The income elasticity of demand for cigarettes appears to be relatively low, a lot less than unity, meaning that cigarette purchases increase by only a fraction of any increase in average incomes. There does appear to be some increase, however.

It has been proposed, in any case, that it is desirable cigarettes be prevented from becoming more 'affordable' in terms of the share of income required for their purchase. That is, tobacco excise rates should be 'indexed' not against general consumer price increases, but in terms of increases in average incomes.

We return to this proposal further on in this report. The relevant statistical evidence is provided in Table A.6. Real income increases, in excess of CPI inflation, are shown for three different income measures.

The three measures show rather different rates of increase, year-on-year and over longer periods. The average rate of increase for the last five years is shown at the foot of the table. The real GDP per head measure is probably too broad in its compass (including in particular the 'profit' component of income), and too subject to later revision, to be used for indexation purposes. Of the 'average earnings' and 'average income' measures, the former has the advantage of already being used for indexation purposes, being an input to annual adjustments of NZ Superannuation pension payments. It shows a lower average annual rate of increase over the last few years (perhaps because of increases in part-time employment) of 1.1 percent

per year. If that rate of increase were maintained, using average earnings as an indexation measure would imply an additional increase in revenues each year, cumulating, of the order of \$10 million x (1- price elasticity), or probably \$3 to \$5 million net each year.

Now Table A.6

A.5 Year-on-Year Real Income Changes

	Real GDP per head	Real Average Weekly Earnings	Real Average 15+ Weekly Income Excl. Inv. Inc.
% change			
1991	-2.9%	0.8%	
1992	-0.6%	1.6%	
1993	3.9%	-0.6%	
1994	4.2%	-0.6%	
1995	2.9%	-1.1%	
1996	2.1%	0.5%	
1997	0.6%	2.4%	
1998	-0.2%	0.5%	
1999	3.5%	2.7%	4.2%
2000	2.3%	-0.9%	-1.7%
2001	2.8%	0.1%	3.6%
2002	3.0%	2.1%	1.3%
2003	2.1%	1.5%	2.7%
2004	2.3%	0.9%	1.8%
2005	1.6%	0.7%	1.2%
2006 (First 3 quarters)		0.9%	
Average 5 years 2000 to 2005	2.4%	1.1%	2.1%

Sources:

CPI Statistics NZ

GDP/head - linked GDP & Resident Population series. Statistics NZ web-site

Weekly Earnings. Qly Employment Survey (QES). SNZ. Labour Market Statistics 2005.

Weekly Income. NZ Income Survey. Stats NZ. Labour Market Statistics 2005

APPENDIX 2

Extract of draft tables and charts, on Tobacco Excises and Customs Excise-equivalent duties

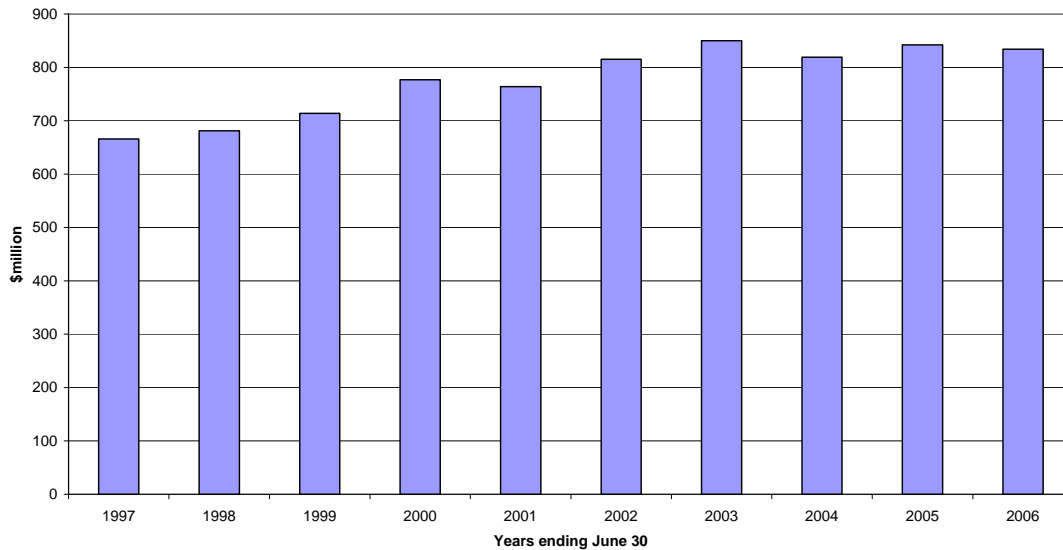
Table A.1	Tobacco Excise Revenue 1996/97 to 2005/06
Chart A.1	Tobacco Excise revenues, 1996/97 to 2005/06, \$million, Accruals basis, GST excluded.
Table A.1a	Tobacco Excise Revenue, including Customs Duty. 1999/2000 to 2005/06.
Table A.2	Real Total and 'Per Smoker' Excise and Customs Duty Revenues. 1996/97 to 2005/06
Chart A.2	Real Excise and Customs Duty Revenues 1996/97 to 2005/06. June 2006 prices, excluding GST
Chart A.3	Real Excise, plus Customs Duties, revenue per smoker 1996/97 to 2003/04. June 2006 prices, excluding GST

A.1 Tobacco Excise Revenue 1996/97 to 2005/2006

\$(million) Excl GST	Years ending 30 June									
	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
Tobacco excise	666	681	714	777	764	815	850	819	842	834
Total tax collected	30,160	31,161	30,227	32,000	34,744	36,215	39,785	42,532	46,624	51,973
Tobacco as % of Total	2.2%	2.2%	2.4%	2.4%	2.2%	2.3%	2.1%	1.9%	1.8%	1.6%

Source: New Zealand Official Yearbook 2004, Table 27.05, Page 454. (Sourced to The Treasury)
Plus Treasury web-site - Tax and Levies Collected (on Accruals basis)

**Tobacco Excise Revenues 1996/97 to 2005/06.
\$million, Accruals basis, excluding GST**



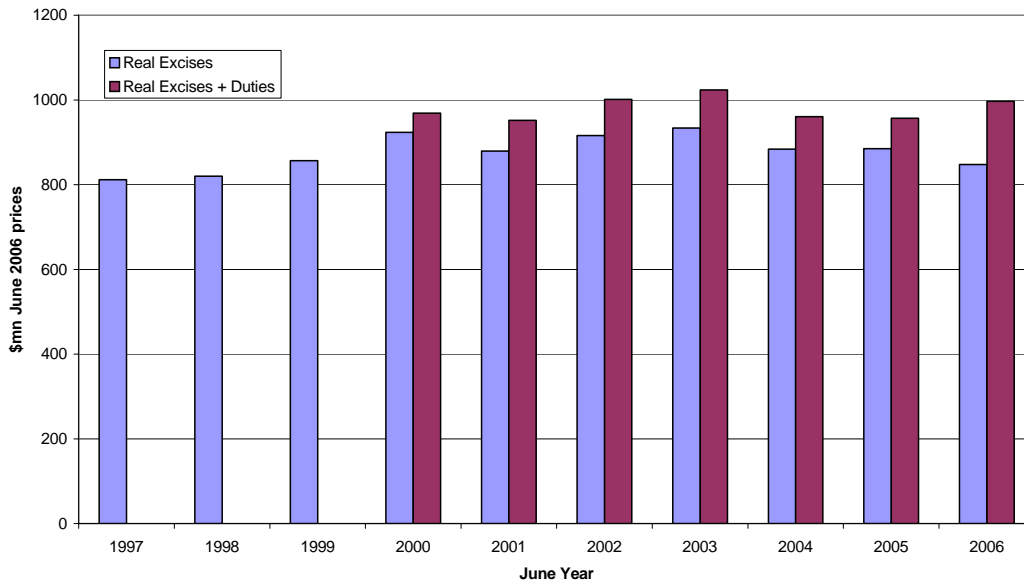
A.2

Real Total and 'Per Smoker' Excise and Customs Duty Revenues. 1996/97 to 2005/2006
 GST excluded.

		Years ending 30 June									
		1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
CPI All Groups. June Qtr 2006 =1000		820	830	834	841	869	890	910	926	951	984
Estimated smokers 15+		752,289	746,241	752,225	757,521	748,675	758,665	773,418	756,452		
Tobacco Excise	Total \$mn	812	820	856	924	879	916	934	884	885	847
	(June 2006 prices) Per smoker \$	1,079	1,099	1,139	1,220	1,175	1,208	1,207	1,169		
Tobacco Excise plus Customs Duty	Total \$mn				969	952	1,002	1,024	961	956	997
	(June 2006 prices) Per smoker \$				1,279	1,271	1,320	1,324	1,270		

Sources: CPI Statistics NZ. Then scaled to new June 2006 base.
 Number of smokers. AC Nielsen survey smoking prevalence rates then applied to total 15+ population.

Real Excise and Customs Duty Revenues 1996/97 to 2005/06.
 June 2006 prices, excluding GST



Real Excise, plus Customs Duty, revenues per smoker 1996/97 to 2003/04.
June 2006 prices, excl. GST

