



# REVENUE VS EXPENDITURE; A CASE STUDY OF TOBACCO TAXES

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## INTRODUCTION

Major environmental and health issues are associated with tobacco consumption. Consumption of tobacco comprises both smoking (roll-ups, cigars, and pipes) and smokeless formulas, all of which pose momentous health perils. The health issues formed by tobacco consumption are nicotine toxicity, pesticide exposure, and musculoskeletal injuries. High death rates caused by prostate cancer are linked with smoking. Additionally, smokers have lower survival rates than other human beings. Research has shown that the harmful chemicals in tobacco not only exacerbate the risks of various cancers, but they also contribute to other chronic health conditions, including heart disease and respiratory illnesses. As awareness of these dangers grows, many countries are implementing stricter regulations to reduce smoking rates and promote healthier lifestyles. The production of tobacco has detrimental effects on ranchers and societies in addition to its consumption. The production of tobacco negatively impacts the environment in such a way that it increases logging, soil attrition, water

effluence, and biodiversity loss. The consumption of tobacco generates negative externalities in the economy. So a Pigouvian tax is the best justification for tobacco taxes. Pigouvian taxes increase the price of tobacco products. Pigouvian tax also highlighted the original social cost of its use to reduce its consumption. Public health theories also promote tobacco taxes to reduce smoking. The demand for tobacco products is inelastic to price. The change in consumption is less than the change in price, but demand for low-income groups and young people shows higher sensitivity to prices. In addition, there are significant social, economic, and developmental costs associated with tobacco smoking, which have a devastating effect on families, communities, and society. According to estimates, smoking costs the economy US\$1.4 trillion annually in 2012, or 1.8% of the world's GDP. The significant negative effects of tobacco smoking on one's health and finances, which are likely to have risen since then, justify government intervention and stringent regulation of the tobacco product market. Beyond

the urgent need to safeguard people's health and welfare, tobacco control should also aim to limit the market failures and adverse externalities associated with tobacco use, especially as these consequences can have a substantial influence on a nation's course for development (WHO report 2023).

Pakistan is a developing country which have to finance its expenditure through revenue generated by taxes. Taxes are the major source of revenue in Pakistan. Taxes on tobacco consumption have also been seen a major source of government revenue. Taxation on tobacco is not only source of revenue for government but it is an effective way to reduce harms caused by tobacco consumption in Pakistan. In Pakistan, both GST and FED taxes were levied on tobacco production and consumption. Historically, Pakistan adopted a tiered tax system. A tiered tax system is a way of taxing different commodities according to their prices. But this system was not so workable in Pakistan because of the negative influence of corporate sectors. Pakistan has abridged its tax structure due to the force of WHO and native community health entities. Pakistan has moved toward a single-tier tax system in 2022. Numerous international commitments have been established to assess the economic impact over the past decade, particularly to deter tobacco usage and non-communicable diseases. These efforts are broadly aimed at reducing demand through pricing and taxation strategies. Global institution which includes WHO IMF and major philanthropic organizations agreed with WHO to accenting and firming the tax on tobacco use as a crucial health policy means. Most of the individuals knows very well that smoking and use of tobacco is very harmful for their health. But there are few who comprehend the gage of this harm.

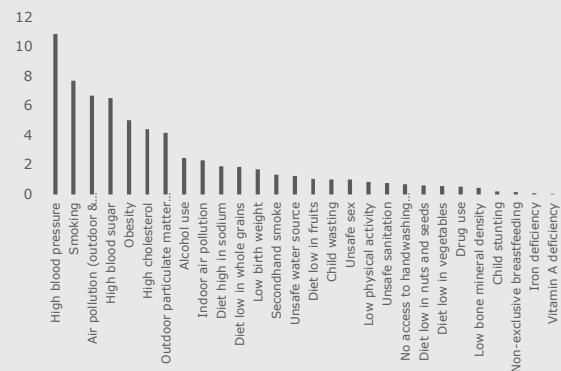
## HEALTH ISSUES AND EXPENSES CAUSED BY TOBACCO CONSUMPTION

More than 100 million of death in previous century were claimed by tobacco epidemic which were due to consumption of tobacco a use of second-hand smoke. This estimate is updated and now reaching 8 million deaths annually by use of tobacco. These estimates are for low- and middle-income countries which shows that how much global burden carried by developing world. Tobacco use causes many long-lasting diseases like cancer, premature deaths, lungs cancer, communally known as NCDs. To gauge the monetary cost of

smoking attributable ailments in 2012, the cost illness approach was used. By using this approach economic cost might be direct or indirect. Direct cost includes hospitals bills whereas indirect cost is the loss of productivity by morbidity and mortality. This approach was employed for 152 countries with including all the essential data which signify 97% of worlds smokers. Health expenditure increases as the consumption of tobacco and smoking increases. Purchasing power parity (PPP) \$467 billion (US\$422 billion) was spent on smoking-related illnesses in 2012, which was accounted 5.7% of all health spending around the world. The yearly monetary cost of smoking was US\$1436 or 1.8 percent of global GDP yearly. Nearly 40% of this expense was incurred in emerging nations, emphasizing the significant burden these nations tolerate.

According to the research, Pakistan's illegal cigarette sales are less than 9%, and the tobacco industry meticulously planned this revenue reduction (likely in 2013) in order to lower the excise rate. Three types of industry actions are highlighted: 1) forestalling, which involves producing more or stock in anticipation of a tax rise; 2) price over shifting, which involves raising the price of cigarettes above the tax rise and 3) overestimating the illegal trade by influencing public and legislators' perceptions.

Deaths (millions)

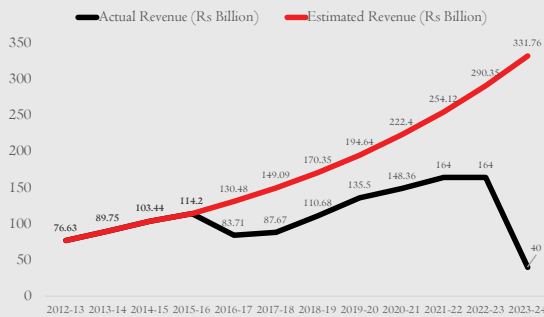


Authors illustration

The Auditor-General of Pakistan (AGP) refuted the FBR's claims about the advantages of establishing the final level of the FED in a report that was sent to the special committee. The implementation of the third tier led to a 31% increase in the turnover of sales for Pakistan Tobacco Company and a 33% increase for Philip Morris International in the fiscal year 2017–18, according to the AGP (ibid). Currently the cost of tobacco use attributable diseases is RS 615.07 billion. RS 437 billion is the total direct and indirect cost which is formed by

cancer, cardiovascular and respiratory diseases. This cost is four times higher than the tax revenue collected by the government on tobacco consumption Nayab et al.

## REVENUE LOSS BY REDUCTION IN TOBACCO CONSUMPTION



During the fiscal period of 2012-2013 the tax revenue of tobacco consumption is RS 76 billion which increased to RS 89 billion in 2013-2014. In 2014-2015 the government met the target of collecting revenue of RS 103.44 billion as previous year. In next fiscal year government collected revenue with 10% YOY growth. Authors illustration

In fiscal year 2019-2020 the tobacco industry generated revenue of RS 110.68 billion in contradiction of the target of RS 194 billion but the actual collection declined by -2.99 percent YOY. The revenue collected by FBR in fiscal year 2021-2022 is RS 135.30 billion against 222.40 billion with more than 22% YOY growth. The tobacco industry's tax was estimated to be RS 290.35 billion in FY 2022-2023, while the actual amount collected was RS 164 billion, representing a 10.33% YOY increase. According to the statistics, the government expected to collect RS 1795.46 billion between 2013 and 2023 (FBR 2023), though the actual amount collected was RS 1228.12 billion. In summary, the tobacco industry's influence caused the government to lose RS 567.34 billion in revenue during this time. The gap is that government has fear of illicit trade due to which it is not putting tax on tobacco industry and lost a huge amount of tax revenue.

## POLICY RECOMMENDATION

Numerous studies and evaluations of the illegal tobacco product trade have shown that strengthening the ability to combat the trade is a more effective strategy to address the issue than avoiding tax increases. Thus, the connection between illicit commerce and good governance must be taken into account. The level of illicit commerce will decrease in a nation with greater capacity to combat it overall. In addition to raising revenue tax policy should work to reduce the consumption of tobacco, it will improve the public health. Government should need to simplify tobacco tax structure, increase impact price level rates and adjust these rates on regular basis to account of economic growth and inflation. Government should excise tax strategy to reduce consumption of tobacco. Because excise taxes have the power to increase both absolute and relative costs, they are the most important taxes imposed on tobacco goods. Increases in the tobacco excise tax also bring in a sizable amount of revenue that will be maintained throughout the short to medium term. Long-term reductions in tobacco use and its effects will be much greater if tobacco taxes are raised further and other evidence-based tobacco control policies and programs are put into place. The implementation of a complete plan to decrease tobacco use maximizes the efficacy of tax increases in accomplishing public health goals, promotes public and political support for higher prices, and results in larger reductions in the adverse effects of tobacco use.



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