

Tobacco Control and the Transitional Economies of Europe: Aspects of Taxation in Poland

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Central and Eastern Europe
Warsaw, Poland



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Raising the “Full Price” of Smoking Participation

- Indirect Costs via Parliamentary Intervention
 - Cost of **Obtaining**
 - Sales restrictions - 1995
 - Advertising/Sponsorship - 1995, 1999
 - Cost of **Consumption**
 - Smoking in Public Places - 1995
 - Counter-Advertising
 - » Tar/Nicotine Content – 1991, 1998, 2000
 - » Health Warning Labels - 1996
- Direct Costs via Fiscal Policy
 - **Monetary** Costs
 - Increase market prices via taxes - 1993



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Tobacco Price Policy via Taxes

- Pre-1993 Turnover Tax System
 - Tax implicit to final price
 - Raise at standard rate of inflation
- 1993 Excise Tax System
 - (1) Specific: size, type, country of origin
 - (2) Ad Valorem: Value-Added Tax (22%)
- 2000 Mixed Excise Tax System*
 - (1) Specific: uniform level across all cigarettes
 - (2) Ad Valorem
 - VAT
 - Variable Excise Tax (25% of retail price) for EU accession*



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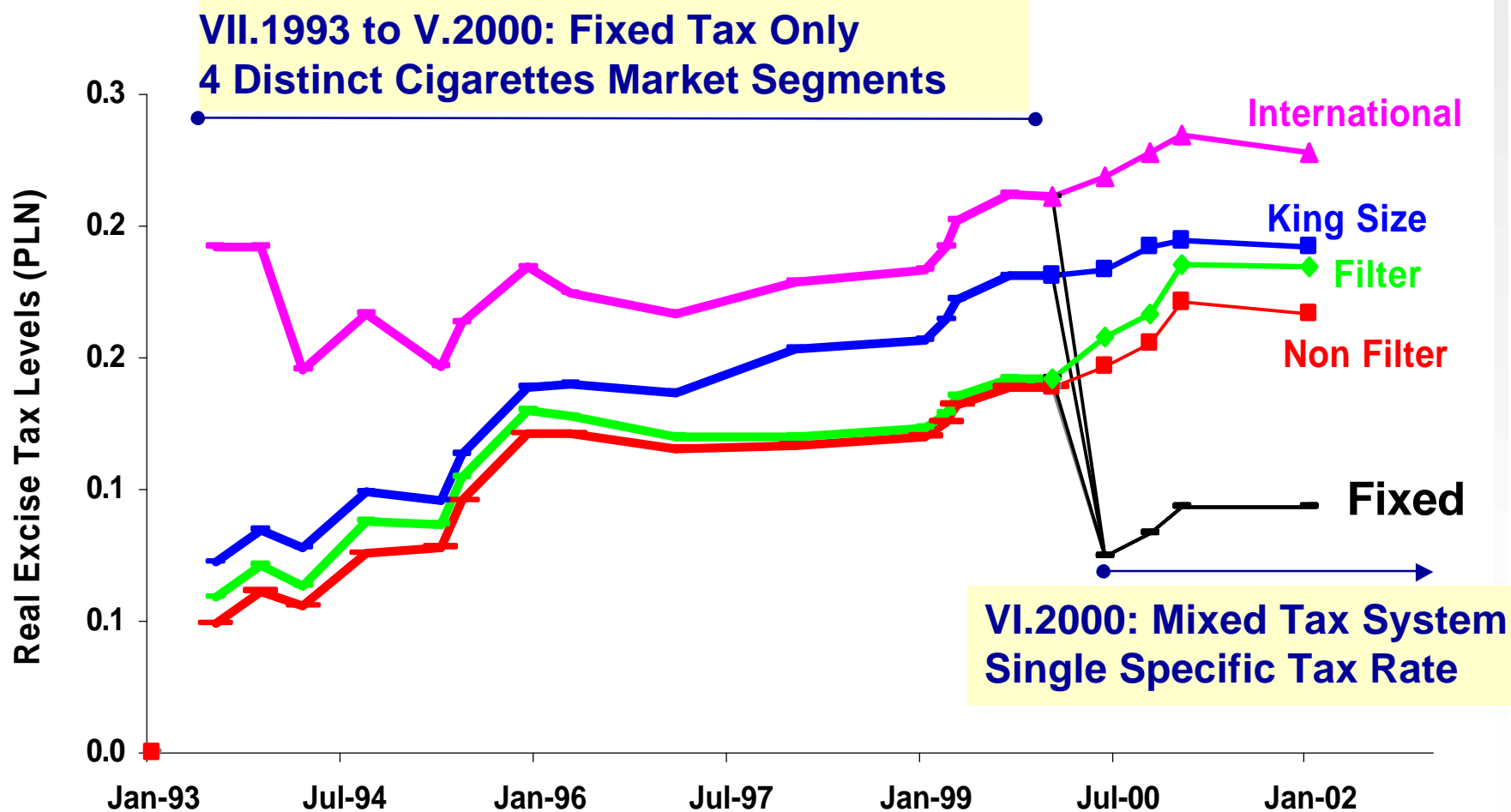
Poland & Accession to EU

- European Union Directive 95/59/EEC
 - (A) Introduction of a **Mixed Excise Duty**
 - **A. Specific: Quantity of Cigarettes**
 - **Fixed Amount/1000 cigarettes**
 - Regularly increase to account for inflation
 - Set by: Ministry of Finance
 - **B. Ad valorem: Value of Cigarettes**
 - **Tax = (%) (Price of cigarettes)**
 - Generally stable as cigarette prices rises with other goods
 - Set by: Parliament
 - (2) Adjustment of the tobacco tax/price ratio to **57%** for cigarette price category most in demand



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(1) Mixed Excise Tax System: Specific + ad valorem

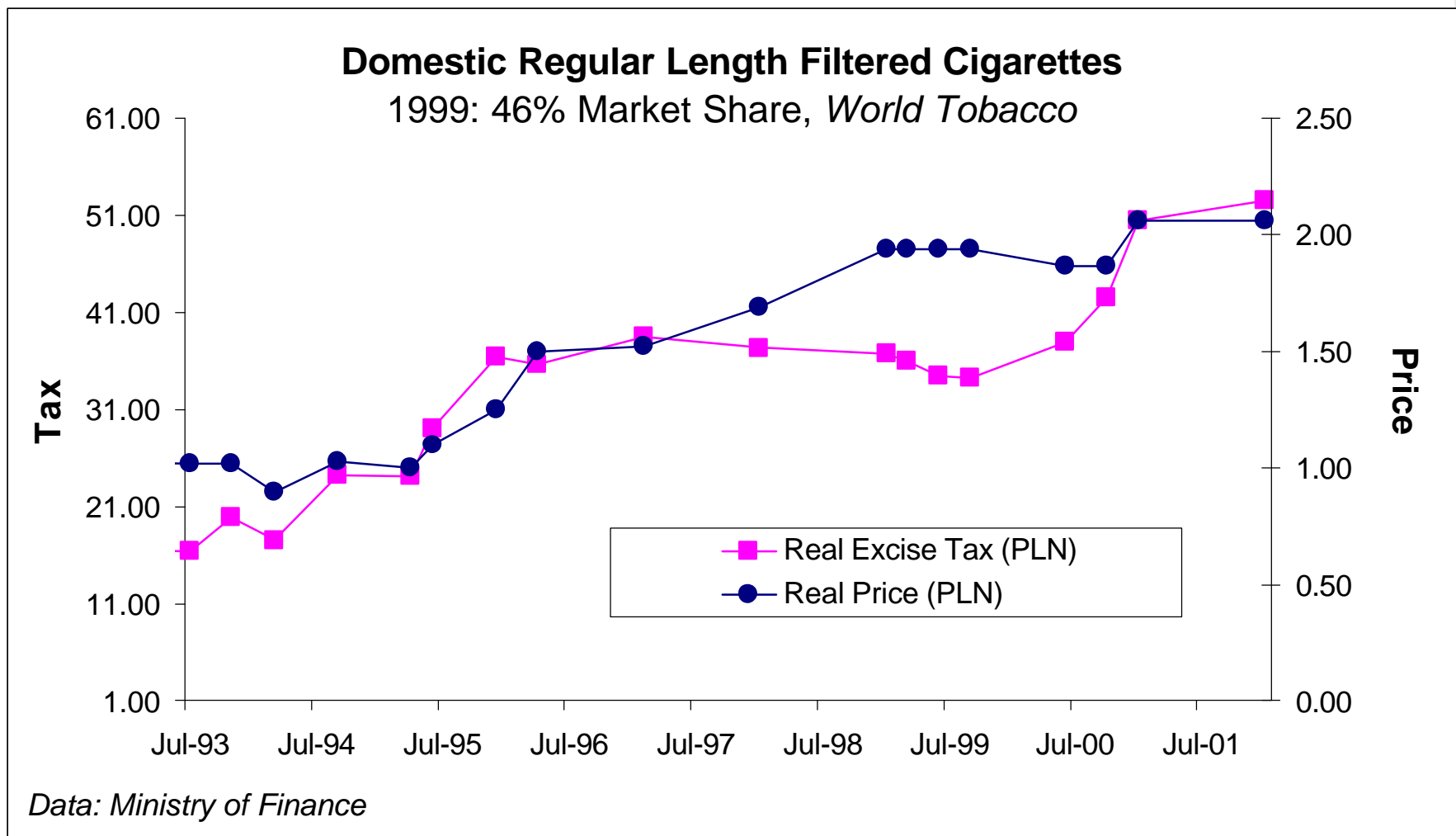


Data: Ministry of Finance



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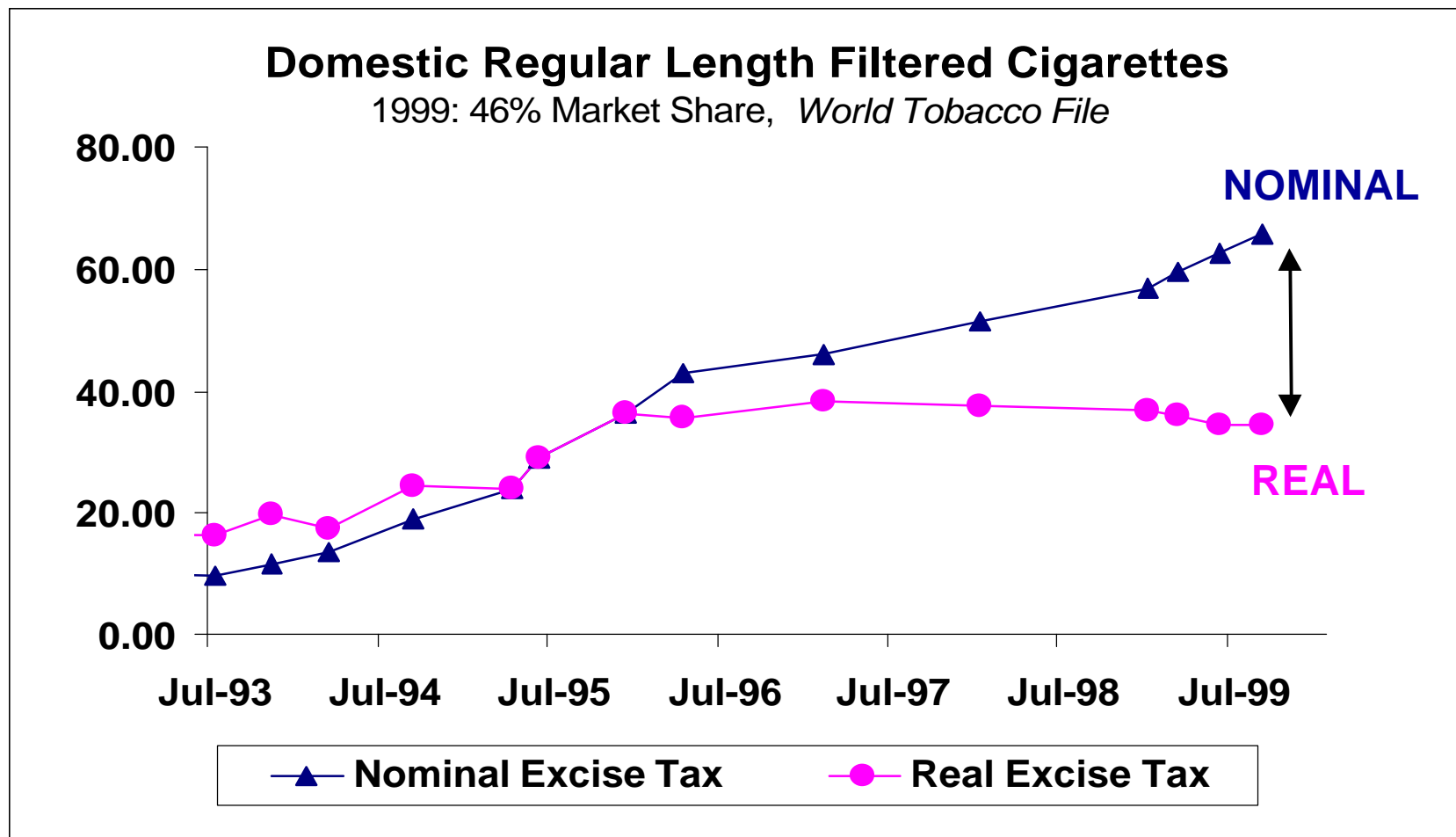
Is Price Rising with Tax?





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Adjust Specific Tax to Inflation



Data: Ministry of Finance



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Ad Valorem's Price Effects

- **In Poland:**

- May 2001: prohibit sales without price label
 - To curb evasion among outlets which attempt to pay lower excise duty by neglecting to reveal final price
 - Manufacturers/importers must provide suggested retail price
- **Ad valorem: opportunity to manipulate total amount of excise tax due!**

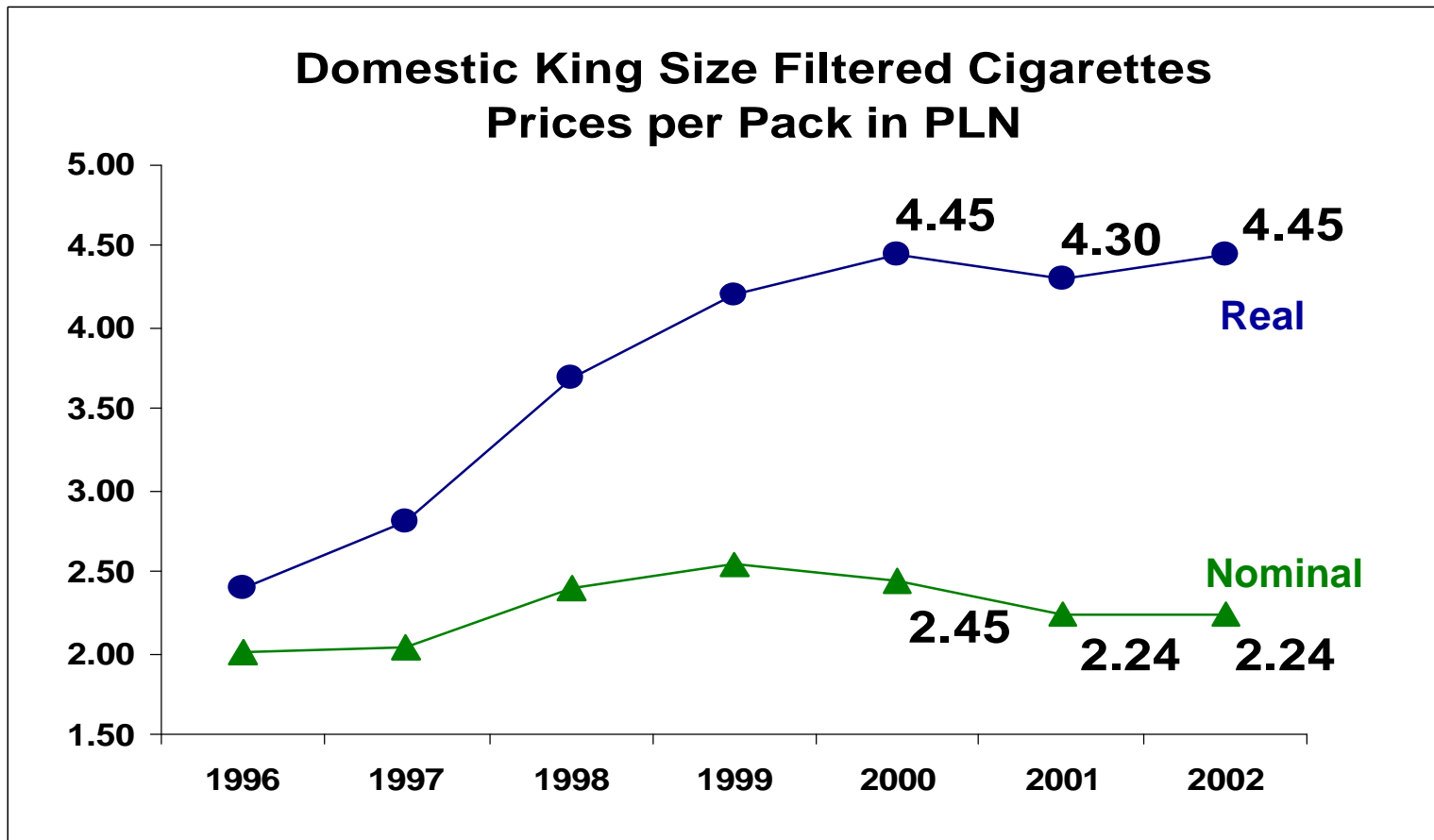
$$\text{Total Tax} = \text{Specific} + 25\% (\text{Retail Price} -)$$





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Price Manipulation?



Data: Ministry of Finance



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Creating Price Incentives.....

	Regular Filter (Klubowe)		King Size (Sobieski)		Regular No Filter (Popularne)		International (Marlboro)	
	Nominal	Real	Nominal	Real	Nominal	Real	Nominal	Real
1997	2.10	1.52	2.80	2.03	1.90	1.38	4.10	2.98
1998	2.60	1.69	3.70	2.40	2.30	1.49	4.75	3.08
1999	3.20	1.94	4.20	2.54	2.50	1.51	5.40	3.27
2000	3.40	1.87	4.45	2.45	2.95	1.62	5.85	3.22
2001	3.95	2.06	4.30	2.24	3.30	1.72	6.00	3.13
2002	4.10	2.06	4.45	2.24	3.30	1.66	6.00	3.02

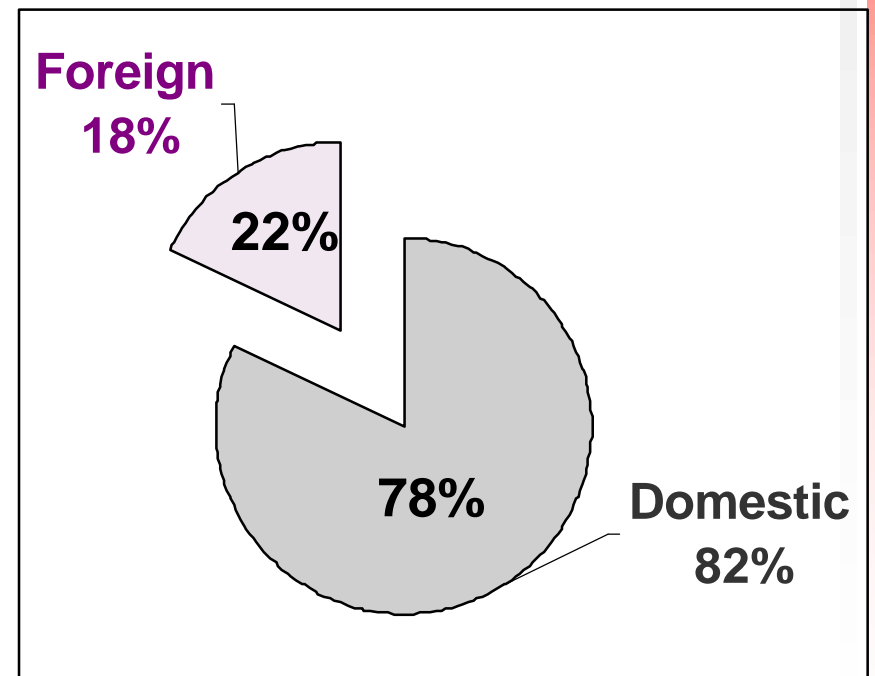
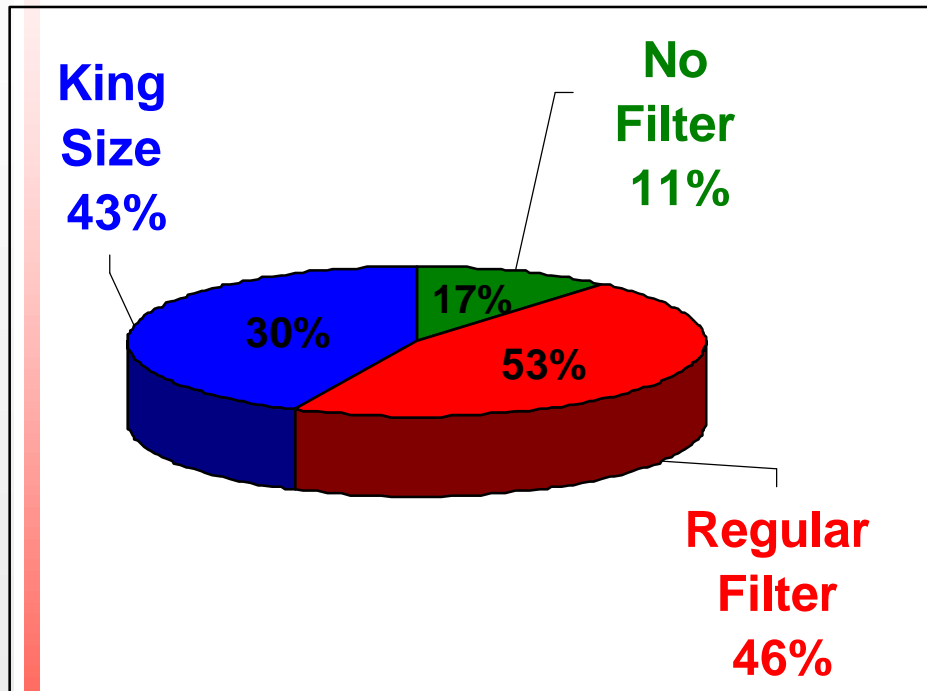
Stagnant or Falling Real Prices in 2001/02!

Data: Ministry of Finance



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..... to drive Market Share?

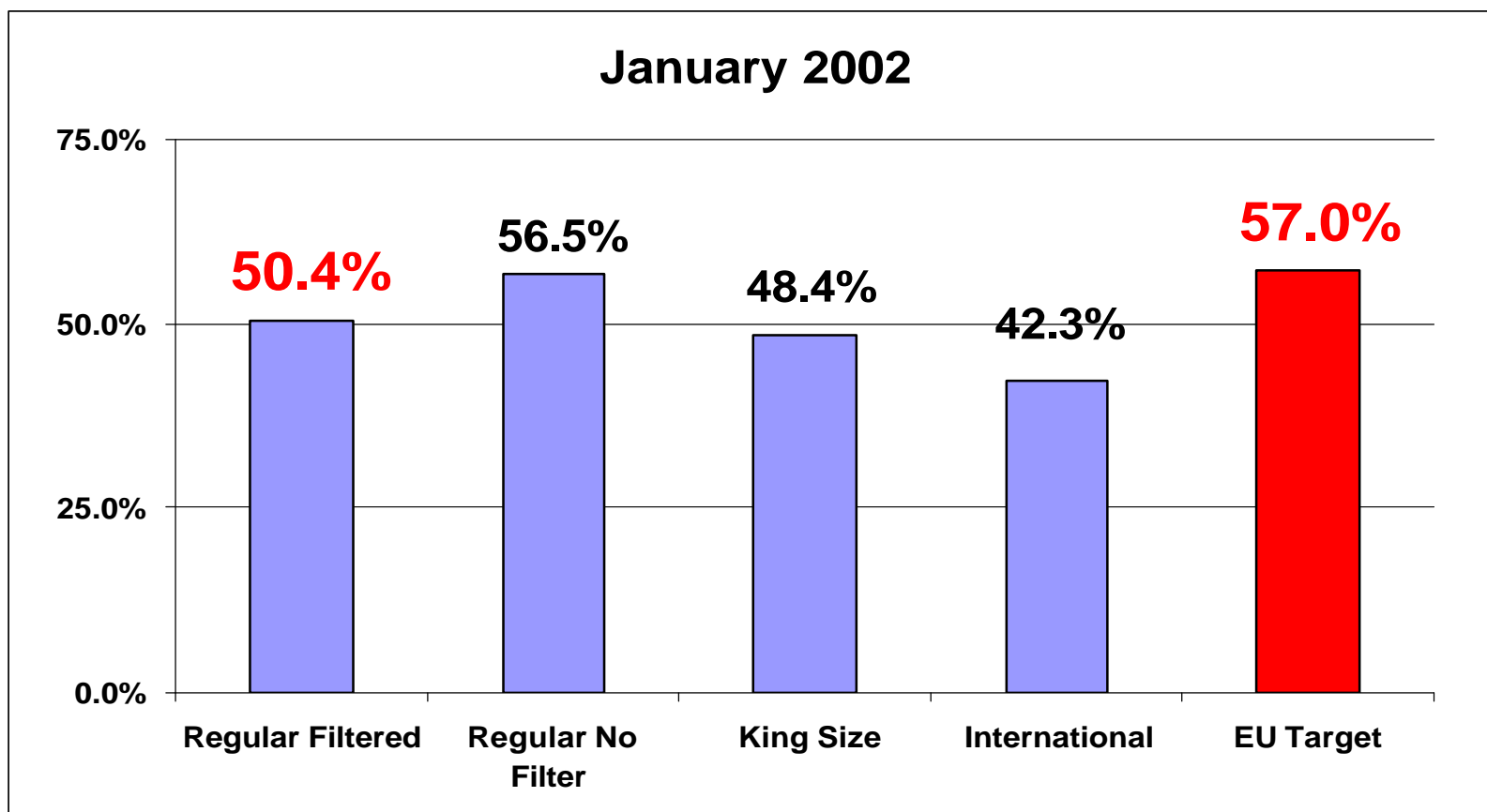


Brand Shares, *World Tobacco* 1996; 2000



(2) Tax to Price Ratio

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Data: Ministry of Finance



Tax Harmonization?

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- Council of Ministers request EU concession
 - October '99: Tax/Price Ratio 41%
- 5 year transitional period until 2004
 - 1) “..requirement of reaching 57% level of excise duty incidence within the short period of harmonization (i.e. by 2002) would lead to several inter-related market occurrences....”
 - 2) “...is desired from the point of view of market stability, state budget income, industry and commerce”
 - 3) “Considering the above **threats**, alignment of Polish legislation with excise duty levels in force in the EU should be effected gradually”.



"Threat" 1

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- "Steep rise in excise duty will result in a retail price increase of 106.9%"

	Tax/Price	Tax/Pack	Price/Pack
Oct-99	41%	1.31	3.20
Jan-02	50%	2.07	4.10
Jan-02	57%		

28%

106.9%
Not Likely

Data: Ministry of Finance, Regular Domestic Cigarettes



"Threat" 2

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- "Inflation level increase due to rapid rise in cigarette prices"
 - 1). Since 1993, CPI reveals **falling** rates:
 - 135.3 in 1993 versus 104.5 in 2002
 - 2). Cigarettes **not** a component of the CPI
 - 3). Assume upper bound (5%) share of monthly household expenditure on cigarettes:
 - $.05 * 16$ or **.8** of an additional CPI point in the month when tax is raised.



“Threat” 3

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- “Decrease in legal cigarette sales due to significant price-sensitivity will result in decreased sales of 33% in 2002 versus 1998”

– Aggregate Demand Model: 1975-2000

- | Annual Consumption/Capita | Coef. | t-stat |
|---------------------------|--------|--------|
| Filter Cigarette Price | -0.082 | -1.860 |
| Annual Income | 0.174 | 1.750 |
| Tobacco Control Law Dummy | -0.071 | -2.450 |

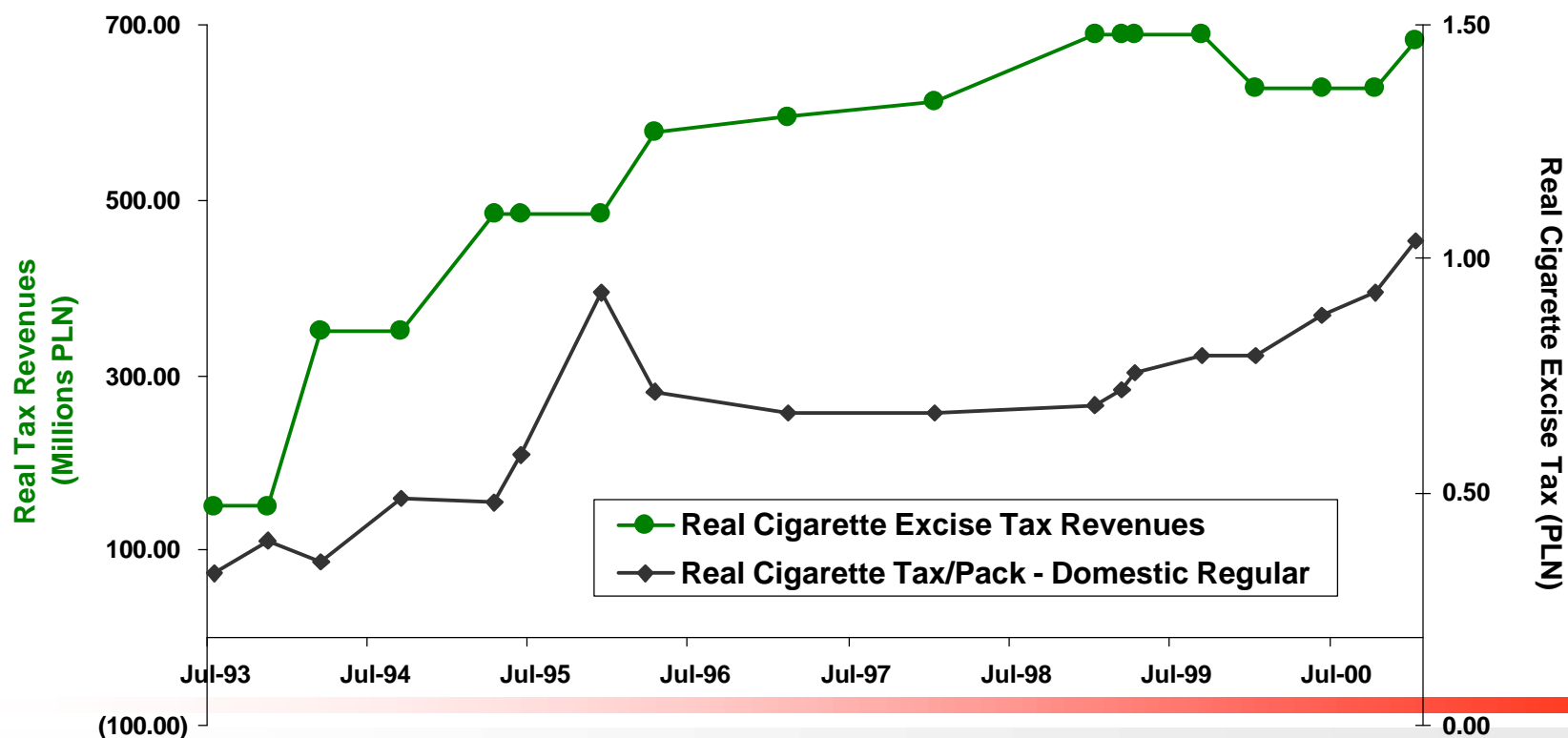
- A 1% rise in Real Cigarette Price lower Cigarette Demand by .8%



"Threat" 4

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- "Decrease of budget income resulting from significant decreases in cigarette sales"





“Threat” 5

Warsaw, Poland

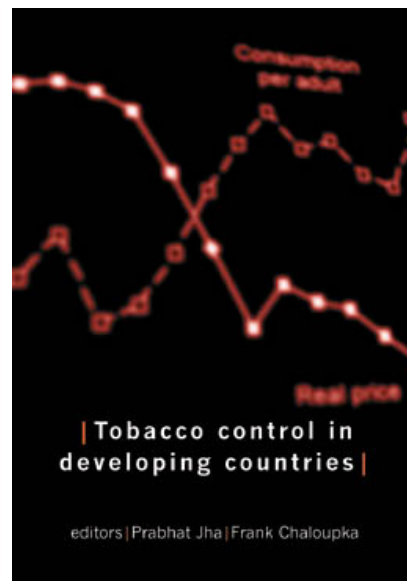
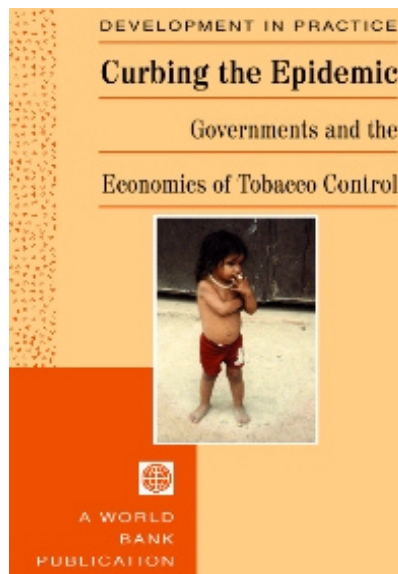
- “Producers forced to limit output and hamper operations and reduce employment”
 - Poland is not heavily dependent on tobacco farming and cigarette production
 - 1995 and 2000 – 8% of manufacturing
 - Falling demand for tobacco \neq permanent loss of jobs
 - Money once spent by smokers on cigarettes will not be spent elsewhere and will create jobs in other economic sectors
 - See Jha and Chaloupka, 1999 and 2000



“Threat” 6

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- “..development of organized cigarette smuggling”
 - Corruption is a stronger predictor of smuggling than price
 - Rather than forgo health benefits of falling smoking rates, take control over smuggling activity in Poland



Jha & Chaloupka, 1999 & 2000



Tax Harmonization? Not Yet!

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DESPITE AVAILABLE EVIDENCE:

EU Member states grant exemption until 2009!