Increasing tobacco taxation revenue in Egypt

World Health Organization
Regional Office for the Eastern Mediterranean

Introduction

The Government of Egypt has been considering expanding the health insurance programme to cover the whole population but given fiscal uncertainties and slow growth in the global economy, the Government has to enhance its revenue base. In addition to other measures, the Government proposed to increase revenue from tobacco taxes, specifically on cigarettes.

In August 2009, as requested by Egypt's Ministry of Finance (MoF), WHO staff from the Tobacco Control Economics programme in headquarters and the Tobacco Free Initiative programme in the Regional Office met with ministry officials to explore possibilities for mutual technical collaboration in the area of tobacco economics and tax. WHO was informed of the Government's plans to introduce an excise system which would replace the general sales tax and introduce a value added tax (VAT) on cigarettes. The objectives of the new tax system were to:

- ensure sustained higher tax revenues.
- eliminate tax avoidance.
- reduce cigarette consumption.
- keep the inflation rate at the same level.

In order to achieve these objectives, the Government considered imposing:

- a mixture of specific and *ad valorem* excises on cigarettes, where the *ad valorem* excise is to be applied on the retail sales price (not on the manufacturers' price).
- 10% VAT on the retail price of cigarettes.
- an increase in the tax rates for other tobacco products (e.g. *shisha*, chewed tobacco).

WHO and MoF collaboration

WHO and the designated team of officials from the MoF worked together to examine Egypt's tobacco tax system and to submit recommendations on how to increase taxes not only on cigarettes but also on other tobacco products and generate more revenue to achieve the above objectives.

To assist in this task an analytical tool, based on the existing system of tax, was developed. The tool considered the market share data of tobacco companies for the last few years, including volume of sales of various cigarette brands, retail prices and the tax structure.

The tool was then used to model the potential fiscal effects of new tax regimes. The MoF team, while considering various options for a prospective tax system, thoroughly studied various tax regimes in other countries. The tool assisted in predicting the possible revenue targets in light of various tax options, price elasticity, inflation and expected changes in volume of sales. The model was finalized in November 2009 and the consequences of increasing tax on tobacco products on the Government's revenues were examined based on data from the MoF, as well as on profits of the Eastern Tobacco Company in which the Government has a 48% share.

In addition to providing direct technical assistance to the MoF, WHO considered it important to develop the capacity of various other governmental and nongovernmental institutions working in tobacco control. Consequently, representatives of WHO visited Alexandria in order to conduct basic tax training to different stakeholders, including academia, the MoF, nongovernmental organizations and advocates in March 2010. During the training, the MoF and WHO team re-examined the model results and discussed alternative tax increases and the consequences of these.

Egypt tobacco prices and tax system before July 2010

Before July 2010, Egypt did not have an excise tax system but relied on a system of general sales tax. General sales tax is levied on domestically produced and imported cigarettes, whereas a modest import duty is levied on imported ones. Part of the revenue from this tax goes to financing medical insurance for students.
The rates of tax were divided into seven tiers, with the rates varying by the manufacturers' or ex-factory price (a net of tax price). Consequently, general

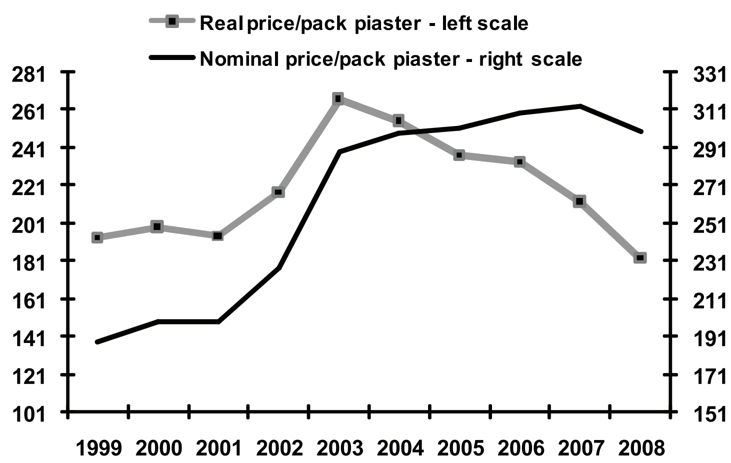
sales tax ranged from LE 1.08 (US$ 0.19) per pack on the lowest priced cigarettes to LE 3.25 (US$ 0.57) per pack on the highest priced ones, with a tax of LE 1.25–1.75 (US$ 0.22–0.31) per pack on the most popular brands.[1]

Regional pricing and tax variations

WHO has been collecting data from various countries to compare the prices of the most popular brands per pack and the taxes levied on those brands (*WHO Global tobacco control report*). During 2008, the price of, and tax on, the most popular brand in Egypt (Cleopatra) was well below that of the most popular brand in other countries of the Region, except Pakistan. Although the tax share in price for the Cleopatra brand is higher than the corresponding one in some other countries (e.g. Djibouti, Islamic Republic of Iran, Iraq, Lebanon, Pakistan, Syrian Arab Republic and Yemen), the Government of Egypt does not earn as much revenue per pack of cigarettes sold as Djibouti, Lebanon and Yemen.

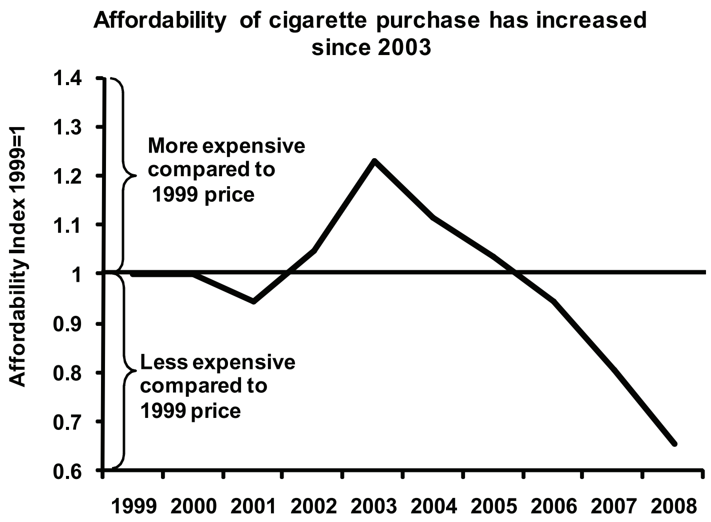
Cigarette prices and consumption patterns

Cigarette consumption has been increasing in Egypt. Per capita consumption increased from 39 packs in 1999 to 47 packs by 2008. One of the leading factors for higher consumption is the declining real prices of cigarettes, as well as declining average retail prices. Although the retail price of cigarettes has been increasing in real terms, the average retail price has been declining since 2003/04 (Figure 1). Since 2003, cigarettes have become more affordable due to higher increases in per capita income (GDP/capita) relative to the increases in retail cigarette prices (Figure 2).



Source: *WHO Global tobacco control report 2009.*

Figure 1. Price of cigarettes and tax share in the Region, 2008



Source: *Tobacco Manufacturing Association 2008, World Economic Outlook 2009.*

Figure 2. Affordability of cigarettes in Egypt, 1999–2008

[1] Exchange rate 1 US$ = LE 5.68

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Tax increase on tobacco products effective 1 July 2010

The MoF submitted a tax proposal to Egypt's Parliament in June 2010. The Parliament agreed to:

- change Egypt's tier tax system to a mixture of *ad valorem* and specific tax system.
- a uniform rate so that all cigarettes would be subject to the same rate of tax.
- a 40% *ad valorem* rate on the retail price of cigarettes plus LE 1.25 (US$ 0.22) per pack specific excise on cigarettes.
- extend the tax increase to cover loose tobacco by 100%.

The new tax change became effective on 1 July 2010.

Implications of the new tax system

- It is estimated that the new tax system will increase the average retail price of cigarettes by 44% from LE 3.51 (US$ 0.62) per pack to LE 5.05 (US$ 0.89) per pack. The highest increase is estimated to take place in mid-priced (49%) and low-priced (45%) brands.
- It is estimated that general sales tax per pack will increase by 87% from LE 1.75 (US$ 0.31) per pack to LE 3.27 (US$ 0.58) per pack while increasing the share of general sales tax on average retail price from 50% to 65%.
- The new tax change would increase general sales tax revenue from cigarettes by 48% from US$ 1200 million to US$ 1760 million. The highest increase is estimated to occur in the mid-priced brand category by 81%.
- The new tax system is estimated to reduce cigarette consumption by 21% to 3078 million packs during 2010–2011 from 3894 million packs in 2009.
- It is estimated that under the pre-July tax system, tobacco would have been responsible for a total of 4.3 million deaths where 2.9 million would be current adults, and 1.4 million would be the youth who would become smokers. Assuming that a third of smokers die prematurely, it is expected that the new tax change will save 498.9 thousand lives in Egypt and 1.8 million smokers will quit smoking given the current prevalence estimates of smoking in Egypt .

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