

The Problem

The current cigarette tax structure (two-tiers of Ksh. 2,630 per mille for cigarette with filters and Ksh. 1,893 per mille for plain cigarettes - is problematic does not align with public health objectives of reducing consumption of tobacco products:

- i. The rates fall way below the World Health Organization (WHO) recommended and therefore promote affordability of tobacco products
- ii. Two rates are likely to inducet substitution from high to low priced brands (switching down) and therefore prevent quitting by consumers
- iii. The introduction of the lower rates has led to loss of government revenue as tobacco industry has developed varieties of their popular brands to conform to this new rate

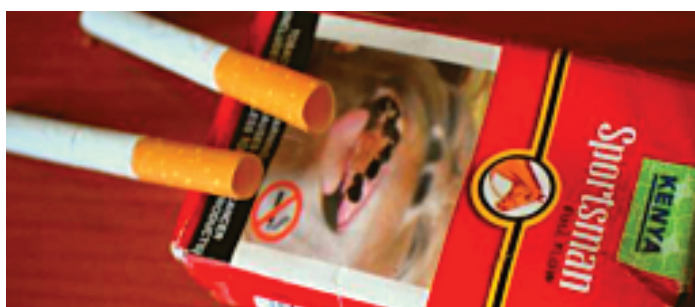


Image 1: A plain/ non- filter cigarette, sportsman 'full flow' introduced by BAT in 2017

1. Background

Tobacco is a leading cause of preventable death globally and it is estimated that by the year 2020, the death toll from tobacco will reach 10 million people; with more than 70% of deaths coming from developing countries (WHO, 2003).

Tax and price measures are considered to be one of the most effective tobacco control strategy due to its potential to discourage initiation, encourage quitting of tobacco use and generate much needed revenue for governments. Tobacco taxes are considered to be an innovative mechanism for financing for development and are therefore a key strategy for the provision of universal health coverage as envisioned under the governments "big four" agenda.

2. Kenya's Excise Tax system

Historically, Kenya has had a complex tobacco tax system and has transitioned severally between specific taxes (1986) to ad valorem (1992). In 1993, a new tiered specific structure was introduced and was based on Retail Selling Price (RSP) with minor adjustments made in certain bands till 2007. Between 2007 and 2010, various models of different excise tax system were used shifting between RSP, product characteristics and/ or packaging characteristics.

The tiered tax structures created incentive for repositioning of brands with some manufacturers reducing the RSP of their lead brands in order to qualify for a lower tax rate, keeping their products cheap, even with regular tax increases, and ultimately inducing smokers to switch to their cheaper brands instead of quitting.

In 2012, the Finance Act simplified the tax structure by reducing the four- tiered specific tax system to a single tier system (at a rate of Ksh. 1200/ mille or 35% of RSP, whichever was higher) and provided for automatic adjustment for inflation .

3. Excise Duty Act 2015

The Excise Duty Act, 2015 was expected to "...deepen tax Administration Reforms and ease compliance" and it introduced a uniform specific rate of Kshs. 2500 per mille. This was a significant step because it introduced a single tier with a specific excise and eliminated the ad valorem. In the two years that the Excise Duty Act, 2015 was implemented, achievements reported include a drop of 17% in consumption of cigarettes and an increase of revenue of approximately 3billion (from 9billion to 12 billion) . However, share of the excise tax in retail price is 44% (and 50% total tax- including VAT), which is still low as compared to the WHO target of 70%.

4. Return of the tiered system FY 2017/ 2018

In his 2017/2018 budget statement, the Minister of Finance reverted back to a tiered system with introduction of two bands of Kshs. 2,500 per mille for cigarette with filters and Kshs. 1,800 per mille for plain cigarettes. This has had the following impact:

Challenges of the Budget Statement 2017/ 18

- ◆ Loss of government revenue due to introduction of non-Governments should use a portion of revenues collected from tobacco taxes to support tobacco control and other health programs in the country in order to reduce the burden caused by the use of this and other harmful products. filter cigarettes, which fall within the lower tax bracket (Ksh. 1,800)
- ◆ Increase in the affordability of cigarettes due lower prices of the new brand of filter-less cigarettes

5. Global Best Practice in tobacco taxation (WHO recommendations for Effective Tobacco tax administration)

Kenya's current tobacco tax structure falls below the WHO recommended best practice as described below:

WHO Recommendations

- ◆ **Excise tax is the most effective type of tax to achieve public health goals and should account for at least 70% of retail price of tobacco products.** At this rate, governments can be assured of price and revenue increases
- ◆ Excise tax increases should **aim to achieve reduction of affordability** and indexed for inflation
- ◆ Simple is better. Complicated systems and structures make tax administration difficult, encouraging tax avoidance and evasion by tobacco companies. Simple structures are more likely to lead to better public health and revenue outcomes.
- ◆ **Specific tax applied to all types & brands of tobacco products are encouraged.** Differential treatment based on specific product price or characteristics often lead to switch from one product to another negating the public health intentions.
- ◆ Low tobacco taxes/ prices **should never be viewed as a 'pro-poor' policy.** Low taxes and prices lead to greater tobacco use amongst the poor hence they bear a disproportionate share of the health and economic burden
- ◆ Governments should **use a portion of revenues collected from tobacco taxes to support tobacco control and other health programs** in the country in order to reduce the burden caused by the use of this and other harmful products.

6. What next for Kenya?

Kenya needs to re- think its tobacco tax structure to not only be in line with the WHO recommendations, but also to promote the Public health and fiscal benefits of effective tax and price policies.

Main Recommendations:

- I. Kenya should Simplify the tobacco tax **structure by re-introducing uniform specific tax rate (single tier) for all cigarettes.**
- II. Kenya should consider making **a significant increase** in the rate of tobacco excise tax*
- III. **All tobacco products should be taxed equally** to prevent tobacco users from switching tobacco brands and types due to price differences.
- IV. The government of Kenya should **consider using a portion of the tax revenue collected to achieve its "Affordable health-care for all" objectives,** under its "big four" agenda.

*Analysis conducted by IILA shows that an increase from Ksh. 2,500 per mille to Ksh. 3,100 per mille of cigarettes would have a positive impact on the consumption rates and revenue levels.

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