

Policy Brief N° 1/2019

Tobacco Taxes
in Latin America

ARGENTINA

ACCELERATING EFFECTIVE
TOBACCO TAXES IN ARGENTINA:
THE IMPACT OF TAX REFORMS

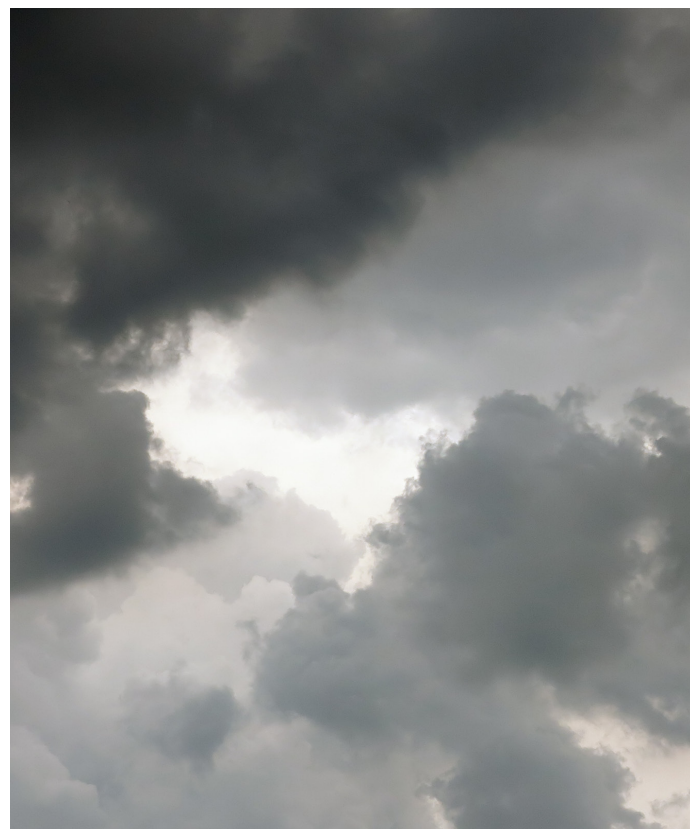
This Policy Brief was elaborated by the South American Network on Applied Economics/Red Sur and presents the main findings and policy recommendations resulting from the background study for Argentina, developed by Instituto Torcuato Di Tella (ITDT/Red Sur), within the UIC- Red Sur project "Tobacco taxes in Latin America", as part of the global project coordinated by The University of Illinois at Chicago's (UIC) Institute for Health Research and Policy and supported by the Bloomberg Initiative to Reduce Tobacco Use.

TOBACCO TAX STRUCTURE IN ARGENTINA

In Argentina, the tax structure surrounding cigarettes is extremely complex and taxes are mostly ad valorem. In the study conducted by the Torcuato Di Tella Institute (ITDT/Red Sur) as part of this project, the effects of the last two tax reforms on cigarette consumption in Argentina are analyzed. The May 2016 tax reform increased the internal tax rate, while the reform contemplated by Law 27.430 of December 2017 introduced a specific tax through the implementation of a minimum tax, updated each quarter for inflation.

The first of these reforms was implemented in May 2016, through Executive Decree 626. This reform established an increase in the internal tax rate on cigarettes from 60% to 75%. This decree was extended by Executive Decree 15/2017 until December of 2017. On that date, the National Congress passed Law 27.430, again modifying the taxes on tobacco consumption. In particular, in the case of cigarettes, the tax rate for internal taxes was reduced from 75% to 70% and a specific tax was introduced, with a minimum of 28 pesos per pack of 20 cigarettes. This minimum tax is adjusted for inflation every three months and the Executive Office has the power to increase the rate by 25% or reduce it by 10%.

The tax burden before the reform of May 2016 was 68.5%. The average retail price in April 2016 was almost 26 pesos per pack of 20 cigarettes, with internal taxes representing 47% of that price¹. After the reform, the tax burden increased and reached nearly 80% in December of 2017. That month, internal taxes represented nearly 61% of the average retail price of almost 50 pesos for a pack of 20 cigarettes.



The second reform of December 2017 was only partially implemented. The minimum tax has yet to be established, meaning that packs of 20 cigarettes remain on the market at values below the minimum tax. The tax burden on a pack of 20 cigarettes -- with an average retail value around 53 pesos -- is 76%. The reduction in the internal tax rate from 75% to 70% resulted in a decrease in the percentage of the retail price made up by these taxes from nearly 61% to 56.2%.

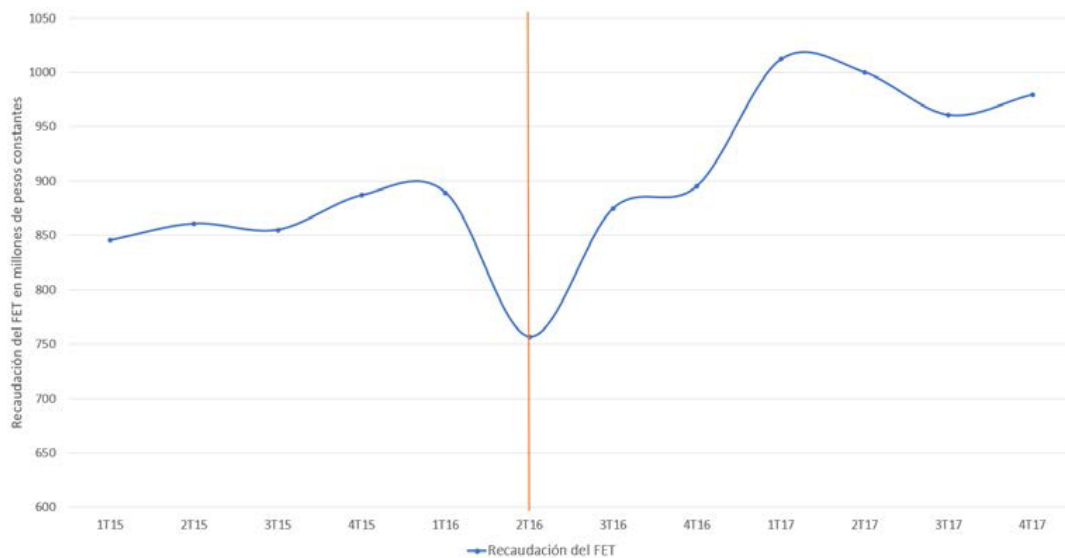
1> The remaining 21.5% of the tax burden was made up of VAT and other taxes with similar characteristics to the internal tax (Special Fund for Tobacco and Additional Emergency Tax).

STUDY RESULTS

To analyze the impact of the reform implemented by Executive Decree 626 of May 2016 on cigarette consumption and State tax collection, a simulation was carried out conducting econometric estimates of tobacco demand.

In the case of Argentina, it's worth noting that funds collected by one of the taxes, the Special Fund for Tobacco (FET), are assigned to tobacco-producing provinces in proportion to the value of their tobacco production. This means that tobacco-producing provinces are generally opposed in the National Congress to any tax reform that may adversely affect these funds. The only selective tax that does not negatively impact the FET is the internal tax.

Figure 1. Tax collection from the FET



X: FET Collection
Y: FET Collection in Millions of Constant Pesos
Para la T de trimestres usar Q (por quarter)
Source: Retrieved from Ministry de Agro-industry figures.



Figure 1 shows tax collection, in millions of constant pesos for the fourth quarter of 2017, coming from the FET before and after the implementation of Executive Decree 626 of May 2016 (represented in the graph by the vertical line). As shown, after the reform that increased the internal tax rate from 60% to 75%, tax collection from the FET increased over the entire period studied.

The study found a long-term elasticity of -0.441, suggesting that a 10% increase in the actual price of cigarettes would decrease consumption around 4.4%. The estimate of short-term price elasticity of demand was -0.911 before the reform of May 2016, while, considering this reform, the absolute value of short-term elasticity increases to -1.385. When the average retail price of the cheapest brands is considered, the implementation of Executive Decree 626 has the effect of transforming short-term price elasticity of demand, meaning that an increase in the actual price of the cheapest brands results in a total decrease in cigarette consumption of 2.2%.

In the case of short-term price elasticity of demand for the most expensive brands, the May 2016 tax reform yields a value of -1.27 and increased the tax burden on cigarettes from 68.5 to 79.7%.

Conversely, the tax reform contained in Law 27.430 of December 2017 has yet to be completely implemented. Several different court filings by the tobacco industry have prevented the minimum tax from being introduced. As a result, 20-cigarette packs with a retail price below the minimum tax of 29.87 pesos remain on the market. Without the implementation of this part of the law, the price gap between inexpensive and expensive brands has remained relatively constant. This evidence suggests that the substitution of inexpensive brands for expensive brands has not occurred. On the other hand, the decrease in the internal tax rate from 75% to 70% resulted in a decrease in the tax burden from 79.7 to 76%.



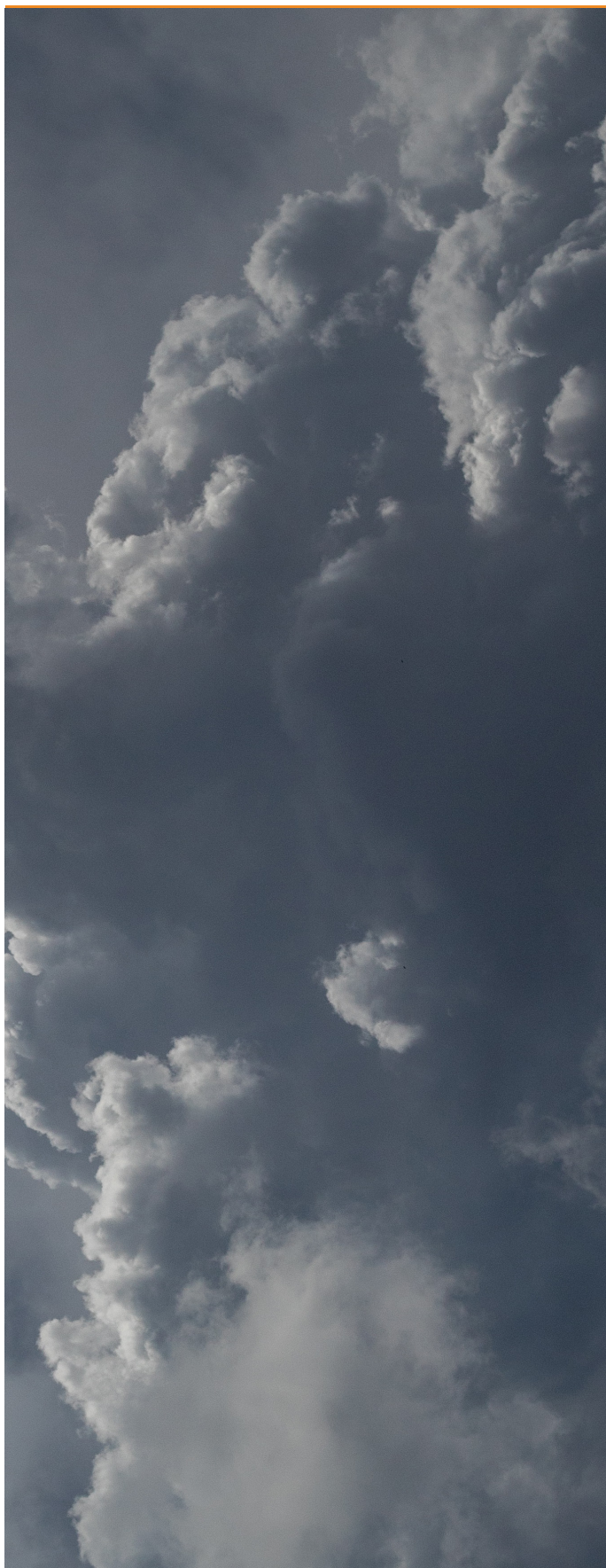
POLICY RECOMMENDATIONS

The results of this exercise suggest that taxes on the consumption of cigarettes can still be increased; thus increasing tax revenue while reducing consumption.

Moreover, the results of the last two tax reforms studied by ITDT suggest that increasing the rate of selective ad valorem taxes yields the most immediate impacts on cigarette consumption and tax revenue, as opposed to implementing a reform with a specific tax as a result of evident institutional pressure through writs of protection, which have managed to thwart attempts to enforce minimum taxes. In particular, the study of both reforms focused on one of the taxes levied on cigarettes: internal taxes. We must keep in mind that, as the different taxes on cigarettes consumption are related, any modification of tax rates impacts the rest of taxes collected.

In conclusion, the results of this study suggest that in Argentina -- due to apparent institutional pressures that have managed, through legal delays, to interrupt attempts to apply minimum taxes -- increasing selective ad valorem tax rates results in more immediate effects on cigarette consumption and tax revenues that implementing a reform that only contains a specific tax.





This Policy Brief was produced based on the background study for Argentina “Accelerating effective tobacco taxes in Argentina: The impact of tax reforms”, developed within the project “Tobacco taxes in Latin America”.

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Within this global initiative, Red Sur led the regional research "**Tobacco taxes in Latin America**", which mobilized seven research centers to study the different options for tobacco tax policies in Argentina, Brazil, Ecuador, Mexico and Peru.

The Project "**Tobacco taxes in Latin America**" was under the Executive Direction of Andrés López (IIEP-BAIRES/FCE UBA, Argentina/Red Sur) and the Coordination of Cecilia Alemany (Red Sur). The Academic Coordination was under the responsibility of a Regional Technical Coordination team, led by Fernando Lorenzo (Centro de Investigaciones Económicas, CINVE/Red Sur) and Oscar Cetrángolo (Instituto Interdisciplinario de Economía Política de Buenos Aires, IIEP-UBA-CONICET/ Red Sur), with the collaboration of Pedro Velasco (UNLP, IIEP-UBA-CONICET/Red Sur) and Carlos Grau (CINVE/Red Sur). The team acknowledges and thanks the comments of Germán Rodríguez-Iglesias (UIC IHRP).

This work's dimensions of analysis were discussed during two research workshops held in Montevideo in 2018, which brought together all national teams, the regional team and the Global Technical Coordination team of Tobacconomics Frank J. Chaloupka, Germán Rodríguez-Iglesias and Erika Siu (UIC IHRP).

No.	Country Study title	Research Team	Center/Country
1	Accelerating effective tobacco taxes in Argentina: The impact of tax reforms	Martín González-Rozada and Julio Berlinski	Instituto Torcuato Di Tella (ITDT/Red Sur) Argentina
2	Accelerating effective tobacco taxes in Argentina: Fiscal and productive aspects	Ricardo Rozemberg, Gabriel Bezchinsky and Ariel Melamud	Centro iDeAS, Universidad Nacional de San Martín (UNSAM) Argentina
3	Accelerating effective tobacco taxes in Brazil: Trends and perspectives	Livio Ribeiro and Vilma Pinto	Fundação Centro de Estudos do Comércio Exterior (FUNCEX/Red Sur) Brazil
4	Accelerating effective tobacco taxes in Peru: Towards sustainable policies	Carlos De los Ríos, Hugo Córdova and Marco Ugarte	Instituto de Estudios Peruanos (IEP) Peru
5	Accelerating effective tobacco taxes in Ecuador: The impact of tax policy	Pedro Páez, Paola Minda, María Dolores Almeida, Ximena Amoroso and Sebastián Burgos	Pontificia Universidad Católica del Ecuador (PUCE) Ecuador
6	Accelerating effective tobacco taxes in Mexico: Tax policy and health costs	Claudia Córdova, Rodrigo Bolaños, Dalia Toledo, Alejandro Alegría and Liliana Alvarado	Laboratorio de Políticas Públicas (ETHOS) Mexico
7	Accelerating effective tobacco taxes in Mexico: Special taxes, consumption, inequality and poverty	Luis Huesca, Linda Llamas, Cuauhtémoc Calderón and Abdelkrim Araar	Centro de Investigación en Alimentación y Desarrollo (CIAD) Mexico

