



# Study on the Excise tax system

*Short Version*

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# Introduction and recommendations for Vietnam

This report summarises the advantages and challenges of the excise tax policy on tobacco products based on the current legal regulations in Vietnam and by acknowledging the proposal put forth by the Vietnam Ministry of Finance (“MOF”) on a new excise tax calculation method using the hybrid method (combination of ad valorem and specific tax to replace the current ad valorem only system). The report also briefly analyzes the effects of the current excise tax policy on the entire tobacco industry and its stakeholders through analysis and assessment of the direct and indirect impacts of the current excise tax policy from different perspectives (e.g. impact on the volume of tobacco consumed, government revenues, the illicit trade as well as the impacts on smoking behaviour and tobacco manufacturers, etc.).

To develop a more appropriate excise tax regime for tobacco than the current policy, this report includes supporting evidence and brief analysis of international practices through various country specific case studies that underwent tobacco tax reform and restructuring measures to meet their own national development goals. The report also analyzes the impacts on the tobacco industry of each excise tax structure (e.g. ad valorem tax structure, specific tax structure and hybrid tax structure) applied in the selected countries. On that basis, the report proposes recommendations on the options for reform of excise tax regime that may be most suitable and feasible for Vietnam in general and the tobacco industry in particular in order to achieve the Government's objectives regarding the management of tobacco consumption, development of the State's revenue, support for the prevention and control of illicit tobacco, protection of consumer rights as well as insurance of the living standards for workers/ farmers in the tobacco industry.

The Government has set the orientation for switching from an ad valorem tax system to a hybrid tax system. This is the right orientation, but the current proposal of the Ministry of Finance will lead to a sudden increase in tax, especially for low-price brands.

In an overall context of Vietnam, we view that any potential increase in the SST should be done on **step by step, at a moderate level; the SST increase plan needs to be long-term oriented with a reasonable roadmap** in order to harmoniously achieve the government's goals on limiting tobacco consumption, while also ensuring the stability of State's revenue, and limiting the sudden increase in illicit trade, thereby transforming the tobacco industry with better quality and less toxic product structure. A tax hike may lead to undesirable reactions from tobacco consumers, namely, switching to more toxic products which are cheaper with lower quality, and especially to the increase in illicit tobacco consumption, which is already a problem in Vietnam. Besides, in the long term, Vietnam should also focus on simplifying the tax structure as simplifying the tax structure lessens the administrative burden for the government, leads to more efficient tax collection and at the end meets the objectives of the Government.

Based on the analysis of Vietnam's current excise tax policy, the objectives of the government with reference to the tax policy of some typical countries (as presented in detail in the full report), the report presents a number of options for reform of excise tax structure together with a short-term roadmap and long-term orientation in line with the current socio-economic situation in Vietnam. With the advantages of the specific tax system, the options presented in the report are based on the orientation that Vietnam will gradually move towards a specific tax system in the long-term (after 10 or 15 years). Overall, the reform roadmap can be implemented in two ways:

**Option 1:** Transitioning into a hybrid tax system then gradually increasing the specific component and decreasing the ad valorem component. In future, it would be considered to move to a single-tier specific tax system when being suitable;

**Option 2:** Transitioning into a multi-tier specific tax system (eg: 4-tier). And then gradually narrow down the number of tiers to become a one-tier specific system.

Detailed examples are shown in the following table.

Option	Roadmap for tax reform
<b>Option 1:</b>	<p><b>(i) In the short term:</b> Transitioning into a hybrid system with the current tax rate at 75% and adding a specific tax rate lower than the one proposed by the MoF (e.g. 500 VND/pack).</p> <p>Since the price range of tobacco products varies, the additional specific tax should be set at a reasonable level. In this example, it is set at 500 VND/pack. For lower-priced brands, this additional specific tax might be acceptable.</p> <p>After that, gradually increase the specific tax component and reduce the ad valorem tax rate so that the portion of specific tax component is gradually increased in the total excise tax.</p> <p><b>(ii) In the long term:</b> gradually moving towards an specific tax system that is more suitable for Vietnam</p> <p>For this option, depending on the orientation and objectives of the Government in the long term, the change in the ad valorem and specific tax components can be implemented quickly or slowly.</p>
<b>Option 1.a: Gradual change of tax</b>	<p>Transitioning into a hybrid tax system with an ad valorem tax rate at the current 75% and adding a specific tax lower than the one proposed by the MoF (e.g. specific tax starts at 500 VND/pack).</p> <p>After every 2 years, the specific tax component is increased by 1,500 VND/pack</p>

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<b>structure</b>	<p>and at the same time, the ad valorem tax rate is reduced by 5% so that the portion of specific tax component is gradually increased in the total excise tax. After 15 years, moving towards a single-tier specific tax system.</p> <table border="1"> <thead> <tr> <th>Scenario 1a</th><th>Excise per pack (VND/pack)</th><th>Current</th><th>Y1</th><th>Y2</th><th>Y3</th><th>Y4</th><th>Y5</th><th>Y6</th><th>Y7</th><th>Y8</th><th>Y9</th><th>Y10</th></tr> </thead> <tbody> <tr> <td>Ad valorem SST (%)</td><td></td><td>75%</td><td>75%</td><td>75%</td><td>70%</td><td>70%</td><td>65%</td><td>65%</td><td>60%</td><td>60%</td><td>55%</td><td>55%</td></tr> <tr> <td>Specific STT (VND)</td><td></td><td>-</td><td>500</td><td>500</td><td>1,500</td><td>1,500</td><td>2,500</td><td>2,500</td><td>3,500</td><td>3,500</td><td>4,500</td><td>4,500</td></tr> <tr> <td>EXP 1 - product A</td><td>7,000</td><td>3,000</td><td>3,500</td><td>3,500</td><td>4,382</td><td>4,382</td><td>5,258</td><td>5,258</td><td>6,125</td><td>6,125</td><td>6,984</td><td>6,984</td></tr> <tr> <td>EXP 2 - product B</td><td>10,000</td><td>4,286</td><td>4,786</td><td>4,786</td><td>5,618</td><td>5,618</td><td>6,439</td><td>6,439</td><td>7,250</td><td>7,250</td><td>8,048</td><td>8,048</td></tr> <tr> <td>EXP 3 - product C</td><td>15,000</td><td>6,429</td><td>6,929</td><td>6,929</td><td>7,676</td><td>7,676</td><td>8,409</td><td>8,409</td><td>9,125</td><td>9,125</td><td>9,823</td><td>9,823</td></tr> <tr> <td>EXP 4 - product D</td><td>25,000</td><td>10,714</td><td>11,214</td><td>11,214</td><td>11,794</td><td>11,794</td><td>12,348</td><td>12,348</td><td>12,875</td><td>12,875</td><td>13,371</td><td>13,371</td></tr> <tr> <td><b>Total</b></td><td></td><td><b>24,429</b></td><td><b>26,429</b></td><td><b>26,429</b></td><td><b>29,471</b></td><td><b>29,471</b></td><td><b>32,455</b></td><td><b>32,455</b></td><td><b>35,375</b></td><td><b>35,375</b></td><td><b>38,226</b></td><td><b>38,226</b></td></tr> </tbody> </table> <p>For illustrative and reference purposes, the above table shows the impact of option 1.a on excise tax collection. This example only shows the effect of excise tax per pack of cigarettes and does not consider the change in consumption due to tax increase, price elasticity of demand or the behaviour of shifting to lower-priced products. The example shows that by implementing a hybrid tax system from year 1 to year 5 with a planned specific tax increase of VND 1500 every 2 years, the excise tax collected by the government is increased steadily with an average growth rate of 4.2% over a 10-year period.</p>	Scenario 1a	Excise per pack (VND/pack)	Current	Y1	Y2	Y3	Y4	Y5	Y6	Y7	Y8	Y9	Y10	Ad valorem SST (%)		75%	75%	75%	70%	70%	65%	65%	60%	60%	55%	55%	Specific STT (VND)		-	500	500	1,500	1,500	2,500	2,500	3,500	3,500	4,500	4,500	EXP 1 - product A	7,000	3,000	3,500	3,500	4,382	4,382	5,258	5,258	6,125	6,125	6,984	6,984	EXP 2 - product B	10,000	4,286	4,786	4,786	5,618	5,618	6,439	6,439	7,250	7,250	8,048	8,048	EXP 3 - product C	15,000	6,429	6,929	6,929	7,676	7,676	8,409	8,409	9,125	9,125	9,823	9,823	EXP 4 - product D	25,000	10,714	11,214	11,214	11,794	11,794	12,348	12,348	12,875	12,875	13,371	13,371	<b>Total</b>		<b>24,429</b>	<b>26,429</b>	<b>26,429</b>	<b>29,471</b>	<b>29,471</b>	<b>32,455</b>	<b>32,455</b>	<b>35,375</b>	<b>35,375</b>	<b>38,226</b>	<b>38,226</b>
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<b>Option 1.b: Rapid change of tax structure</b>	<p>Start with a hybrid tax system similar to option 1.a. However, the roadmap for change of ratio of the specific and ad valorem components is faster. Example: After every 2 years, the specific tax component is increased by 2,000 VND/pack of cigarettes and ad valorem tax rate is reduced by 15%. After 5 times (about 10 years), moving towards a single-tier specific tax system.</p> <table border="1"> <thead> <tr> <th>Scenario 1b</th><th>Excise per pack (VND/pack)</th><th>Current</th><th>Y1</th><th>Y2</th><th>Y3</th><th>Y4</th><th>Y5</th><th>Y6</th><th>Y7</th><th>Y8</th><th>Y9</th><th>Y10</th></tr> </thead> <tbody> <tr> <td>Ad valorem SST (%)</td><td></td><td>75%</td><td>75%</td><td>75%</td><td>60%</td><td>60%</td><td>45%</td><td>45%</td><td>30%</td><td>30%</td><td>15%</td><td>15%</td></tr> <tr> <td>Specific STT (VND)</td><td></td><td>0</td><td>500</td><td>500</td><td>2,500</td><td>2,500</td><td>4,500</td><td>4,500</td><td>6,500</td><td>6,500</td><td>8,500</td><td>8,500</td></tr> <tr> <td>EXP 1 - product A</td><td>7,000</td><td>3,000</td><td>3,500</td><td>3,500</td><td>5,125</td><td>5,125</td><td>6,672</td><td>6,672</td><td>8,115</td><td>8,115</td><td>9,413</td><td>9,413</td></tr> <tr> <td>EXP 2 - product B</td><td>10,000</td><td>4,286</td><td>4,786</td><td>4,786</td><td>6,250</td><td>6,250</td><td>7,603</td><td>7,603</td><td>8,808</td><td>8,808</td><td>9,804</td><td>9,804</td></tr> <tr> <td>EXP 3 - product C</td><td>15,000</td><td>6,429</td><td>6,929</td><td>6,929</td><td>8,125</td><td>8,125</td><td>9,155</td><td>9,155</td><td>9,962</td><td>9,962</td><td>10,457</td><td>10,457</td></tr> <tr> <td>EXP 4 - product D</td><td>25,000</td><td>10,714</td><td>11,214</td><td>11,214</td><td>11,875</td><td>11,875</td><td>12,259</td><td>12,259</td><td>12,269</td><td>12,269</td><td>11,761</td><td>11,761</td></tr> <tr> <td><b>Total</b></td><td></td><td><b>24,429</b></td><td><b>26,429</b></td><td><b>26,429</b></td><td><b>31,375</b></td><td><b>31,375</b></td><td><b>35,690</b></td><td><b>35,690</b></td><td><b>39,154</b></td><td><b>39,154</b></td><td><b>41,435</b></td><td><b>41,435</b></td></tr> </tbody> </table> <p>For illustrative and reference purposes, the above table illustrates the impact of Option 1.b on the excise tax rate/pack. With the same assumptions as in option 1.a, excluding the impact of consumption quantity, price elasticity of demand, or consumers' shift to lower-priced products, with the implementation of a hybrid tax system from year 1 to year 10 with a planned increase in specific tax of VND 2,000 every 2 years and a 15% decrease in ad valorem every 2 years, government revenue from excise tax is increased steadily with an average growth rate of 4.2% over the 10-year period, same as option 1.a</p> <p>The roadmap for tax reform should be made public so that enterprises can develop suitable business plans, especially those that are manufacturing low-price tobacco.</p> <p>Depending on the orientation of the Government and the market structure, the adjustment of ad valorem and specific tax components in the tax structure will</p>	Scenario 1b	Excise per pack (VND/pack)	Current	Y1	Y2	Y3	Y4	Y5	Y6	Y7	Y8	Y9	Y10	Ad valorem SST (%)		75%	75%	75%	60%	60%	45%	45%	30%	30%	15%	15%	Specific STT (VND)		0	500	500	2,500	2,500	4,500	4,500	6,500	6,500	8,500	8,500	EXP 1 - product A	7,000	3,000	3,500	3,500	5,125	5,125	6,672	6,672	8,115	8,115	9,413	9,413	EXP 2 - product B	10,000	4,286	4,786	4,786	6,250	6,250	7,603	7,603	8,808	8,808	9,804	9,804	EXP 3 - product C	15,000	6,429	6,929	6,929	8,125	8,125	9,155	9,155	9,962	9,962	10,457	10,457	EXP 4 - product D	25,000	10,714	11,214	11,214	11,875	11,875	12,259	12,259	12,269	12,269	11,761	11,761	<b>Total</b>		<b>24,429</b>	<b>26,429</b>	<b>26,429</b>	<b>31,375</b>	<b>31,375</b>	<b>35,690</b>	<b>35,690</b>	<b>39,154</b>	<b>39,154</b>	<b>41,435</b>	<b>41,435</b>
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	<p>be made accordingly. The basic matter is to avoid sudden adjustment so as not to cause disturbance to the market.</p>																																																																																																								
<b>Option 2:</b>	<p><b>Short-term:</b> Transiting from an ad valorem tax system to a multi-tier specific tax system based on the thresholds of ex-factory prices.</p> <p>Because the range of retail and ex-factory prices of tobacco products in Vietnam is quite wide with a wide range of products. However, in general, they can be divided into the following 4 groups:</p> <ul style="list-style-type: none"> <li>• Group of low segment (20.8% market share - 2021)</li> <li>• Group of value for money segment (48.2% market share - 2021)</li> <li>• Group of aspirational premium segment (12.7% market share - 2021)</li> <li>• Group of premium segment (6.3% market share - 2021)</li> </ul> <p>The specific tax rate can be set at the corresponding rate. For example:</p> <table border="1"> <thead> <tr> <th>Scenario 2</th> <th>Excise per pack (VND/pack)</th> <th>Current</th> <th>Y1</th> <th>Y2</th> <th>Y3</th> <th>Y4</th> <th>Y5</th> <th>Y6</th> <th>Y7</th> <th>Y8</th> <th>Y9</th> <th>Y10</th> </tr> </thead> <tbody> <tr> <td>Ad valorem SST (%)</td> <td>75%</td> <td>0%</td> </tr> <tr> <td>Specific STT (VND)</td> <td>0</td> <td>4 bâc</td> <td>4 bâc</td> <td>4 bâc</td> <td>4 bâc</td> <td>4 bâc</td> <td>2 bâc</td> <td>2 bâc</td> <td>2 bâc</td> <td>2 bâc</td> <td>2 bâc</td> <td>2 bâc</td> </tr> <tr> <td>EXP 1 - product A</td> <td>7,000</td> <td>3,000</td> <td>3,000</td> <td>3,000</td> <td>4,000</td> <td>4,000</td> <td>6,000</td> <td>6,000</td> <td>7,000</td> <td>7,000</td> <td>8,000</td> <td>8,000</td> </tr> <tr> <td>EXP 2 - product B</td> <td>10,000</td> <td>4,286</td> <td>5,000</td> <td>5,000</td> <td>6,000</td> <td>6,000</td> <td>6,000</td> <td>7,000</td> <td>7,000</td> <td>7,000</td> <td>8,000</td> <td>8,000</td> </tr> <tr> <td>EXP 3 - product C</td> <td>15,000</td> <td>6,429</td> <td>7,000</td> <td>7,000</td> <td>8,000</td> <td>8,000</td> <td>11,000</td> <td>11,000</td> <td>12,000</td> <td>12,000</td> <td>13,000</td> <td>13,000</td> </tr> <tr> <td>EXP 4 - product D</td> <td>25,000</td> <td>10,714</td> <td>11,000</td> <td>11,000</td> <td>12,000</td> <td>12,000</td> <td>11,000</td> <td>11,000</td> <td>12,000</td> <td>12,000</td> <td>13,000</td> <td>13,000</td> </tr> <tr> <td><b>Total</b></td> <td><b>24,429</b></td> <td><b>26,000</b></td> <td><b>26,000</b></td> <td><b>30,000</b></td> <td><b>30,000</b></td> <td><b>34,000</b></td> <td><b>34,000</b></td> <td><b>38,000</b></td> <td><b>38,000</b></td> <td><b>38,000</b></td> <td><b>42,000</b></td> <td><b>42,000</b></td> </tr> </tbody> </table> <p>For illustrative and reference purposes, the above table illustrates the impact of excise tax per pack of option 2. With the same assumptions as in option 1, excluding the impact on consumption volume, price elasticity of demand or consumer's shift to lower-price products, the illustration shows that if a 4-tier specific tax system were implemented immediately, the excise tax collected by the government will be increased steadily with an average growth rate of 5.6% over the 10-year period, slightly higher than options 1.a and 1.b. However, once again, illustrative figures do not consider potential adverse reactions from stakeholders, which could happen if the tax system is changed suddenly with immediate effect as in this case.</p> <p>Since Vietnam is not able to monitor the retail price, the calculation of tax rate still uses the ex-factory price as currently.</p> <p>Every one or two years, the specific tax should be adjusted due to inflation. The government can issue a roadmap for tax increase so that enterprises can develop their appropriate business plans.</p> <p><b>Long-term:</b> Gradually build a roadmap to simplify the tax structure, reducing from four-tier to three-, two- or one-tier depending on the development of the</p>	Scenario 2	Excise per pack (VND/pack)	Current	Y1	Y2	Y3	Y4	Y5	Y6	Y7	Y8	Y9	Y10	Ad valorem SST (%)	75%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	Specific STT (VND)	0	4 bâc	2 bâc	EXP 1 - product A	7,000	3,000	3,000	3,000	4,000	4,000	6,000	6,000	7,000	7,000	8,000	8,000	EXP 2 - product B	10,000	4,286	5,000	5,000	6,000	6,000	6,000	7,000	7,000	7,000	8,000	8,000	EXP 3 - product C	15,000	6,429	7,000	7,000	8,000	8,000	11,000	11,000	12,000	12,000	13,000	13,000	EXP 4 - product D	25,000	10,714	11,000	11,000	12,000	12,000	11,000	11,000	12,000	12,000	13,000	13,000	<b>Total</b>	<b>24,429</b>	<b>26,000</b>	<b>26,000</b>	<b>30,000</b>	<b>30,000</b>	<b>34,000</b>	<b>34,000</b>	<b>38,000</b>	<b>38,000</b>	<b>38,000</b>	<b>42,000</b>	<b>42,000</b>									
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EXP 3 - product C	15,000	6,429	7,000	7,000	8,000	8,000	11,000	11,000	12,000	12,000	13,000	13,000																																																																																													
EXP 4 - product D	25,000	10,714	11,000	11,000	12,000	12,000	11,000	11,000	12,000	12,000	13,000	13,000																																																																																													
<b>Total</b>	<b>24,429</b>	<b>26,000</b>	<b>26,000</b>	<b>30,000</b>	<b>30,000</b>	<b>34,000</b>	<b>34,000</b>	<b>38,000</b>	<b>38,000</b>	<b>38,000</b>	<b>42,000</b>	<b>42,000</b>																																																																																													

Option	Roadmap for tax reform
	market.

The above options all generate revenue growth for the government regardless of other factors such as effects on quantity, price, price or discount elasticity of demand. However, with a moderate increase in tax following a clear roadmap, the negative impact on the market will be minimised.

Each of the options mentioned above has its own advantages and disadvantages, but in general, we believe that option 1 is more reasonable for the current situation of Vietnam when gradually transitioning from the ad valorem tax system to a hybrid tax system structure in the short term without immediately transitioning into a four-tier specific system like in option 2. This option is also consistent with the reform orientation of the MoF. The main difference is that instead of increasing taxes suddenly, the increase in tax is made gradually according to the roadmap so that enterprises and the market can adapt gradually. For option 1, the combined implementation of a lower specific tax rate than currently proposed by the Ministry of Finance will help avoid a sudden increase in the price of legal tobacco products, which affects the consumers and will lead them to shift to cheaper tobacco including poor quality, toxic tobacco with an unknown origin, and illicit tobacco.

However, in the long run, we suppose that the specific tax structure is better than the hybrid or ad valorem tax structure because the collection of tax will be based on the quantity of tobacco consumed. The specific tax structure may help to avoid the big difference between the ex-factory price and retail price that may occur with the ad valorem or hybrid tax structure. In order for a smooth transition to the specific tax system, the Ministry of Finance should consider gradually increasing the component of specific tax and reducing that of the ad valorem tax to encourage the investment in improvement of product quality. Thus, the difference in tobacco prices will gradually be reduced and the complete transit will be performed when it is suitable.

The Government may also not apply the hybrid tax structure due to the complication in tax declaration and calculation and transit immediately to the specific tax structure. Due to the big difference in the prices of tobacco products, a tiered specific tax structure (starting at four-tier) by price segment (from the current price segments of premium, aspirational premium, value for money and low, as referred from retail price to producer price) as proposed in Option 2 will be more suitable to the Vietnamese market.

This tax regime will help achieve the Government's goals in a balanced way while minimising fluctuations on the tobacco industry, supporting all segments and restricting the sudden drop in quantity, thereby reducing the negative social impacts on consumers, farmers and workers. In the long run, the Government may consider moving towards a simpler specific tax structure (e.g. two-tier) that is more suitable for Vietnam, then maybe even towards a single specific

tax rate to ease the burden of tax administration and tax collection and to stabilise revenue and make it predictable.

When studying tax policies of the typical countries in the world, we find that such countries tend to apply a specific tax structure, especially in the Asia Pacific region. The specific tax structure has been successfully implemented in many countries and can bring benefits to the government with regard to stabilising revenue, simplifying administrative procedures and easily adjustable against inflation. This structure also helps to stabilise the business environment in the industry, stimulate competition and provide more choices to consumers.

Below is a brief comparison of the pros and cons of the two proposed reform options:

Option	Pros	Cons
<b>Option 1</b>	<ul style="list-style-type: none"> <li>- Easier for the Vietnamese government and manufacturers to accept because in the short term, the adjustment in ad valorem tax rate is relatively small while the specific tax rate is applied at a lower rate than currently proposed and will gradually increase following to a clear roadmap</li> <li>- A lower increase in tax than currently proposed one will lead to a slight increase in retail prices and reduce consumers' shift to cheaper tobacco products or illicit tobacco, thereby limiting loss of tax revenue.</li> <li>- The time for the transition to a specific tax system can be adjusted depending on the orientation and the goals of the government. Option 1.b can allow a faster transition to a specific tax system than Option 1.a because of the higher adjustment rate for each time.</li> </ul>	<ul style="list-style-type: none"> <li>- The high component of specific tax may not be well received by all stakeholders.</li> </ul>
<b>Option 2</b>	<ul style="list-style-type: none"> <li>- Allows faster transition to a specific tax system</li> <li>- Stimulates fairer competition for enterprises in the industry and provides better balance of excise tax for all products</li> </ul>	<ul style="list-style-type: none"> <li>- Sudden change for a tax system is not simple and easy, considering a number of its positive and negative impacts on different stakeholders.</li> </ul>

# I. Overview of the current tax regime in Vietnam

## 1. Background

Vietnam currently uses a uniform 75% ad valorem tax system on all tobacco products. At the end of 2017 and the beginning of 2018, the Vietnam Ministry of Finance (MoF) proposed reforming the excise tax on cigarettes by proposing to adopt a hybrid system that includes a ad valorem tax and a specific tax (also known as the hybrid system) to replace the prevailing ad valorem tax system<sup>1</sup>. Option 1 is to apply excise tax by the hybrid method (both ad valorem tax rate and specific tax) by adding the specific tax of 1,000 VND/pack of 20 cigarettes and 1,500 VND/a cigar. This regulation is proposed to be applied from 2020. Option 2 proposed by the Ministry of Finance is to increase the tax rate according to the roadmap, from 2020, the tax rate will increase from 75% to 80%. From 2021, the tax rate will increase to 85%. Stated its point of view, the Ministry of Finance said that the method of combining ad valorem tax and specific tax was adopted by many developed countries (about 48 countries). Therefore, the Ministry of Finance proposes option 1. However, the amendment of the Tax Law has been delayed since 2017 for the reason that it needs to be studied further with the participation of stakeholders. MoF is expected to conduct research and reform of excise tax soon.

In the research to amend the Law on Excise Tax related to tobacco products, a number of objectives set by the Government need to be considered carefully, including:

- To implement the Framework Convention on Tobacco Control, including the recommendation: *"Member countries should implement the most simple and effective tax system that is suitable for their financial and national health objectives. The Members should consider implementing a specific or hybrid tax system with a minimum specific tax rate, as these tax systems are more advantageous compared to a simple ad valorem tax system."*
- *Decision No. 508/2022/QD-TTg dated April 23, 2022 approving the tax reform strategy to 2030 states that the excise tax reform strategy for the period 2021-2030 is: "developing a tax adjustment roadmap for tobacco products, beer, wine, automobiles, etc. in order to control consumption and fulfil international commitments;... studying the application of a combination of ad valorem tax and specific tax for some taxable goods and services".*
- Reduce the smoking rate in (i) young people (aged from 15 to 24): from 26% in 2011 to 18% by 2020; (ii) Men: from 47.4% in 2011 to 39% by 2020 and to 37% by 2025; and (iii) Women: to below 1.4% by 2020.<sup>2</sup> Currently, there is no target for the next phase.
- Along with the goal of **reducing smoking rates to protect public health**, the Government also requires **control of illicit tobacco and counterfeit tobacco**, as outlined in the "Overall strategy for Vietnam's tobacco industry to the year 2010 and vision for 2020". Specifically: *"Increasing the inspection and control of the transportation, trade of illicit tobacco, supporting financially using the state budget*

<sup>1</sup> [https://mof.gov.vn/webcenter/portal/btcvn/pages\\_r/l/tin-bo-tai-chinh?dDocName=MOFUCM109989](https://mof.gov.vn/webcenter/portal/btcvn/pages_r/l/tin-bo-tai-chinh?dDocName=MOFUCM109989)

<sup>2</sup> *Decision No. 229/QD-TTg dated January 25, 2013*

*and contributions of tobacco manufacturers to prevent and repel illicit tobacco and supporting to equip means and human resources for anti-illicit-trading forces”.*

Therefore, it can be seen that in addition to the goal of tax reform for increasing state revenue from tax in a sustainable way, the goal of protecting public health through reducing the quantity of tobacco consumed and the rate of smokers is considered more important. The new tax system, other than meeting objectives of government revenue and public health, also needs to avoid causing sudden changes to the market in order to balance the objectives for reduction of consumption quantity with the control of illicit tobacco and counterfeit tobacco, and balances with the potential negative social impacts of the new policy such as the risk of sudden unemployment for tobacco workers and farmers, and at the same time gradually shift the product lines from the low segment to the mid and premium segment.

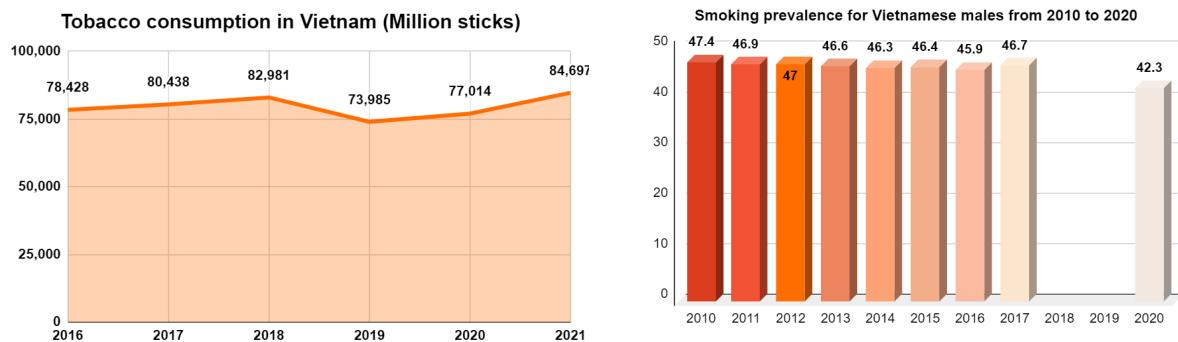
## **2. The shortcomings of the current excise tax system (ad valorem tax structure on the manufacturers’ selling price)**

In general, we believe that the current excise tax structure needs to be further improved to meet the objectives set by the Government and stakeholders. We would like to briefly present an overview of the analysis of the impact of the current tax regime on relevant socio-economic factors as a part of the fundamental reason why the current excise tax policy needs to be improved:

### ***(2A) Not enough effectiveness to control tobacco consumption in the long term***

Data from recent surveys shows that more than one-fifth of Vietnamese adults aged 15 and above are smokers, with men making up the majority. The latest survey on Vietnam's tobacco consumption shows a decline in consumption after the most recent tax hike in 2019. Consumption rate continued to be low in 2020 before showing signs of a slight increase in early 2021. This trend is in line with tobacco consumption in the same year as data shows a recovery in tobacco consumption in the first quarter of 2021 following the Covid 19 economic shutdown in 2020. Therefore, we believe that although the market recovery may partly explain why tobacco consumption increased in 2021, the current tax policy may not be effective enough to consistently control tobacco consumption over the long term.

In the National Strategy for Tobacco Harm Prevention, the Vietnam Government has set out some measures and set a target to reduce the rate of tobacco consumption among men to 39% by 2020, to 37% in the period from 2022 to 2025; and 32.5% by 2030. However, the statistical results show that the rate of male smokers will remain at 42.3% in 2020, only slightly down from 46.7% in 2017 and 47.4% in 2010.



Therefore, the current excise tax policy for tobacco is not the main factor affecting tobacco consumption in Vietnam and does not support the Vietnamese Government in sustainably controlling reduction of tobacco consumption. Current smoking rates among Vietnamese men remain high and exceed the government's target rate (actual smoker rate of 42.3% in 2020 compared to target rate of 39% in 2020). Thus, the tobacco consumption needs to be further controlled and the roadmap to increase excise tax has not yet met the reduction target as was set out.

### **(2B) Many inadequacies in the prevention and control of illicit tobacco are revealed**

According to the Asia Illegal Tobacco Index (2017), more than 24.3 billion illicit cigarettes are consumed in Vietnam due to their competitive prices and easy accessibility. In 2017, an estimated 23.4% of total tobacco consumption in Vietnam was illicit. This results in an estimated total tax loss of about 5.3 trillion VND (i.e. 235 million USD).

Based on Neilson's statistics for the period 2019-2021, major players in the industry such as Vinataba, other tobacco manufacturers in the Vietnam Tobacco Association and other multinational tobacco companies have lost about 15-20% of their market share to the illicit tobacco market. Apart from this loss, the market share of legal tobacco especially in the 'Premium and Aspirational premium' segments continued to decline, while the share of illegal tobacco increased sharply by 29% and 13% respectively, after the increases in tax rate in 2016 and 2019.

According to estimates in the industry, the trend shows that tax increases since 2016 have accelerated the consumption of illicit tobacco in Vietnam across all product segments. The increase in illegal tobacco consumption in Vietnam can be seen from two main factors: (i) illicit tobacco into Vietnam are not subject to high import tax (135%), plus excise tax and VAT, and (ii) Vietnamese smokers normally consider the illicit products are "foreign products" - which could have higher quality than domestically produced products. A good example is that, for the most popular premium tobacco brand like '555' which has a long history in the Vietnamese market, illicit products are believed to have higher quality when compared to premium domestically produced products or other taxable premium brands. Besides, illicit tobacco often does not include the graphic health warning labels, so most smokers prefer and are willing to pay at a higher price for the illicit tobacco. Thus, once the

SST increases suddenly, the price gap between the illicit products and the legal products will be reduced, resulting in more smokers choosing the illicit products due to its “foreign” perception.

From these trends, it can be concluded that the current tobacco tax structure:

- does not encourage domestic manufacturers to improve the quality of their tobacco (since tobacco is taxed based on cost, manufacturers will tend to keep prices low). Therefore, when retail prices increase suddenly, abolishing the difference between legal and illicit tobacco, most consumers will tend to shift to tobacco from illegal sources or cheaper products.
- has promoted the price gap between legal and illicit tobacco, especially for the low segment that are likely to be consumed by lower-income smokers.
- The increase in excise tax with the current tax policy will not be able to correspond to the income growth rate and inflation rate, leading to the continued increase in illegal tobacco trade. In addition, it is clear that the sudden increase in tax will likely cause a trend to decrease consumption, facilitating the consumption of illicit tobacco, and most likely will cause loss of Government revenue. Because illicit tobacco is easily accessible to consumers, it destroys price efficiency and tax regulations aimed at reducing consumption.
- The long border with Cambodia and Laos, the inherent tendency of consumers (in particular, to prefer foreign tobacco) will add to the difficulties for Vietnam. Besides, illicit cigarette trade has been normalised, leading to its extensive access into the market. Therefore, to effectively fight the illegal trade, more resources are needed to be mobilised to tighten border control and market management, especially in border provinces

The analysis also shows that the problem of illicit tobacco continues to leave a negative impact on the Government and public health sectors in Vietnam, especially affecting the effectiveness of the measures regarding price and tax initiated by the Government to restrict tobacco consumption. More specifically, we suppose that, with the current tax structure, an increase in the tax rate may increase the quantity of illicit tobacco, despite some illicit control measures implemented by the government.

#### ***(2C) Not really supporting to create stable and sustainable budget revenue for the Government***

Since 2005, studies from the Global Tobacco Control Program of World Bank Group and estimates of the industry indicate that despite a gradual increase in nominal revenue, the total tax revenue from tobacco of the Government does not increase after being adjusted for inflation. Actual budget revenue from excise tax for tobacco remains the same without

increasing in line with the trend of inflation. The two main reasons why the real government real revenue has increased consistently with the inflation rate are:

- Retail prices may not keep up with inflation
- Downtrading behaviour and high-level illicit tobacco

It can be seen that excise tax revenue from tobacco has not increased in recent years, which proves the above point that the current tax system may not be effective enough to help increase revenue for the Government. Therefore, to generate growth and a stable and sustainable revenue, the Government should consider reforming the tax system to reflect the current fiscal environment in Vietnam and should study how other countries are pursuing reform or modification of the tobacco tax structure.

***Non-encouraging manufacturers to invest to improve the quality of tobacco products and unwanted effects on social security***

Statistics show that the increases in tax rate in 2016 and 2019 has caused a decrease to the quantity of tobacco manufactured in Vietnam, especially in the latest increase in 2019. This is evidence from the most serious decrease in revenue and output of domestically manufactured tobacco of many decades, leaving a significant impact on the activities of enterprises and workers in the tobacco industry. The downturn continues to 2021, partly due to the impact of COVID-19, as well as the prevalence of illicit cigarettes in the market. Therefore, the current tax structure and the inconsistent policy changes have led to undesirable impacts on production activities and social security.

Practically, for an ad valorem tax system, any increase in the ex-factory price or the cost of the product is passed on to the consumer at a rate higher than the one-to-one ratio resulting in a higher retail price due to the multiplier effect. However, with the current tax structure, manufacturers, importers and consumers will likely try to minimise tax payments by cutting down their costs. Therefore, businesses have no motivation to improve the quality of cigarettes or tobacco leaves with the current tax structure. Manufacturers tend to buy cheaper tobacco from farmers or from neighbouring countries, rather than investing in improving the quality of the leaves. This motivates illicit tobacco traders and further worsens the dropout situation in the country as this tax structure does not motivate farmers or local producers to improve the quality of domestically grown tobacco leaves.

## II. Research on international experience and some typical cases in the world

### 1. Common experiences of countries on excise tax reform

Currently in the world, according to WHO statistics in 2021<sup>3</sup>, countries tend to switch to applying the specific or hybrid excise tax structure (increase by 22.5% from 102 countries in 2008 to 125 countries in 2018 - accounting for 69% of the countries in the statistics). Meanwhile, the number of countries applying ad valorem tax structure decreased by 25% in the above period (from 55 countries to 41 countries). Countries also tend to reform from a complex tax structure to a simpler one in order to simplify management and easily adjust to inflation and predict government revenue.

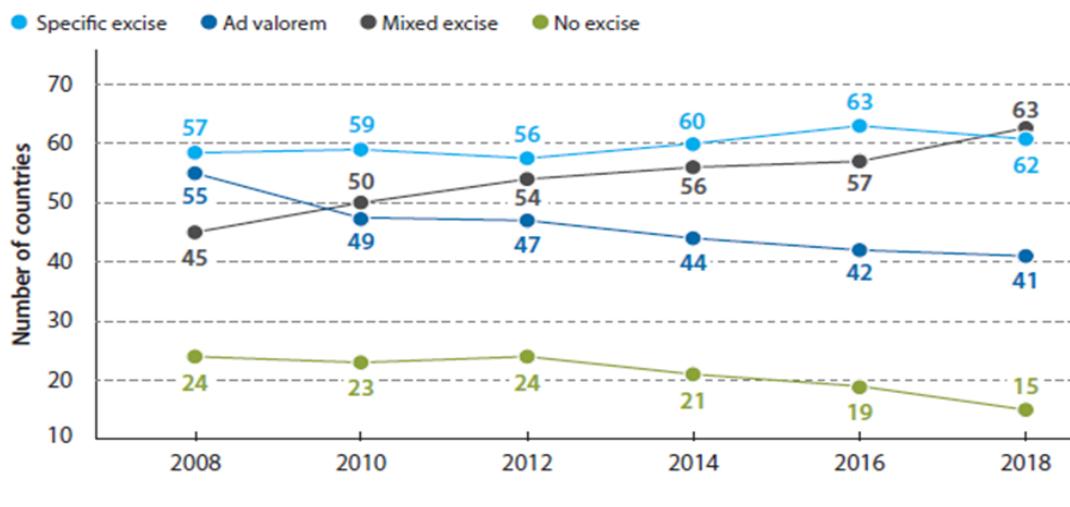


Chart: Global tax structure trends

Source: WHO 2021

In addition, policy makers of countries around the world must constantly pay attention to potential factors that can cause negative impacts in the process of implementing each model of excise tax on cigarettes and continue to simplify the tax structure to best suit the industry of their country. An effective excise tax policy is one that is easy to manage and helps policymakers and tax authorities to accurately forecast revenue sources. An appropriate tax structure also needs to contribute to improving transparency in tax collection, improving actual tax revenue, and stabilizing the tobacco market, without increasing the risk of tobacco smuggling. According to WHO, the design of tobacco tax policy should prioritize simplicity, and a single-tier specific tax structure is the best tax structure because it can be easily adjusted regularly following inflation and income growth. Simplifying the excise tax structure on tobacco will facilitate tax administration, reduce opportunities for tax avoidance and evasion, increase revenue, and have a greater impact on reducing tobacco use.

<sup>3</sup> WHO (2021), Technical manual on tobacco tax policy and administration (accessed online in June 2022)

Beside that, through analysis and research on tobacco consumers around the world, any excessive excise tax increase will push up the retail price of legal cigarettes, drive consumers away from legal products and force them to look for cheaper alternatives through illegal channels. Therefore, a sudden or excessive tax increase in a short time will not reduce smoking consumers as the Government's goals and expectations, on the contrary, only shift consumers from using legal products to illegal tobacco products. This will create negative social effects such as job losses, while government revenues become unstable and, in some cases, may decrease.

In the future, WHO recommends that countries that currently apply ad valorem tax should, first, start transitioning to a hybrid system by adding a specific tax component or introducing a minimum Tobacco Excise Tax Rates. Meanwhile, countries that are adopting a hybrid system consisting of ad valorem tax and a specific tax should consider increasing the specific tax component frequently, so that the specific tax component takes a larger portion in total excise tax (before switching to a pure specific tax system).

As such, it can be seen that the above step-by-step tax reform roadmap can also be applied to Vietnam, with the goal of reducing ad valorem tax portion, and at the same time, initially introducing the specific tax component (possibly starting from a lower level in the short term) before converting to a single tier specific system in the long run. To ensure a smooth transition, Vietnam should first consider implementing a hybrid structure without the need for an abrupt shift to a specific multi-tier or even a single tier specific system.

## **2. International case studies**

This section will provide highlights from the 7 selected international case studies. For ease of reference, we categorise the case studies into best practices which were illustrated in the cases of Germany, the Republic of Korea, the Philippines, where the simplified tax structure and a gradual tax increase created predictable government revenue flows and a more balanced tax system.

In addition, we also analyse the UK and Malaysia cases as typical examples of countries that have the excessive increase of excise taxes, leading to an increase in the retail price of legal cigarettes and driving consumers to seek cheaper alternatives through illegal channels. This causes serious consequences such as loss of government tax revenue, closure of legal tobacco factories and increased unemployment of workers in the industry. Indonesia is a country with a complex tax structure that leads to some undesirable results and is in the process of reforming to simplify the tax structure.

## 1. Germany

Please refer to detailed information and information sources at page number 37 - Full version of the Study on Excise Tax System.

<b>Overview and Status</b>	<p>Excise tax structure: Hybrid (ad valorem tax and single-tier specific tax)</p> <p><b>Excise tax policy over time:</b></p> <ul style="list-style-type: none"><li>• Period 2002-2005: The German government applied several tax increases both on the ad valorem and specific components during the 4-year period causing the retail prices of tobacco products to increase significantly. As a result, the tax hike during the period drove consumers to non-domestic cigarettes (both legal and illicit) from other countries resulting in their volume being doubled in the period while legal cigarette consumption decreased by around 34%<sup>4</sup> and resulting in stagnant budget revenue.</li><li>• Period 2006 - 2010: The German government decided to slightly increase the excise tax in one time for tobacco products during this period but still not improving the consequences from the previous period.</li><li>• Period 2011-2015: The excise tax had been adjusted to gradually increase for over a 5-year period. The average budget revenue since the model's implementation (from 2011 to 2019) has increased for more than 4.2% compared to the period from 2006 to 2010, at the same time, tobacco consumption decreases by about 3% per year for all tobacco products.</li><li>• Stabilization period 2016-2021: Although the excise tax remains unchanged compared to the immediate previous period, the excise tax collection has increased regularly at a moderate rate and the domestic illicit tobacco trade has also decreased sharply.</li><li>• In summary, from 2005 onward to 2021: the ad valorem tax component started to decline gradually while the specific tax component after being frozen for a certain period began to increase steadily. This highlights the trend of greater use of the specific tax component and a gradual decline in the use of the ad valorem tax component. With this trend, Germany was able to achieve its goal of increasing government revenue as well as continuing to decline in consumption.</li></ul>
<b>Experience</b>	<ul style="list-style-type: none"><li>• Excessive excise tax increase leads to large increases in the retail prices of</li></ul>

<sup>4</sup> Benjamin Kuntz, Johannes Zeiher, Cornelia Lange and Thomas Lampert, 'Trends in Tobacco Sales in Germany, Journal of Health Monitoring' 2017 2 (2).

<b>for Vietnam in excise tax reform</b>	<p>legal cigarettes, which encourages consumers to find the alternatives such as cross-border shopping for cheaper products, or illegal tobacco products. As a result, the government lost revenue significantly while increasing its illegal trade and cross-border trade problems.</p> <ul style="list-style-type: none"> <li>● A gradual and moderate increase in excise tax in a specific period will make it easier to manage and predict budget revenues and at the same time help effectively control the trade and consumption of smuggled tobacco.</li> </ul>
<b>2. Republic of Korea</b>	
	<p><b>Please refer to detailed information and information sources at page number 41 - Full version of the Study on Excise Tax System.</b></p>
<b>Overview and Status</b>	<p>Excise tax structure: single-tier specific tax</p> <p><b>Excise tax policy over time:</b></p> <ul style="list-style-type: none"> <li>● In 1989: the excise tax system was changed from ad valorem tax to a specific tax.</li> <li>● Period 1996-2015: Korea implemented many tax reforms and tax increases on both cigarettes and alternative tobacco products. The most recent tax hikes were in 2005 and 2015<sup>5</sup>, the Korean government implemented tax increases when cigarettes became more affordable and applied an excise tax to reduce tobacco consumption. Consumption fell sharply in the year of tax reform, at the same time tobacco tax collection by the government also increased over the past two decades.</li> <li>● Tobacco tax reform in 2015 led to a significant tax increase on all tobacco products. The percentage of excise tax on the price of a cigarette pack rises from 62% to 74%. As a result, the price of a cigarette pack significantly increased by 80% (from 2,500 won per pack to 4,500 won). As a result of tax reform, tobacco consumption fell sharply in 2015 at 23.7% compared to 2014 while government tax revenue increased at 20% and 49% in 2015 and 2016 compared to 2014.</li> </ul>
<b>Experience for Vietnam in</b>	<ul style="list-style-type: none"> <li>● Korea has a relatively simple tax structure (i.e. single tier specific tax) that is not reliant on pricing strategy but rather on the consumption unit. This structure allows the Korean government to better predict the tax revenue and design an</li> </ul>

<sup>5</sup> World Bank. 2018. Reducing tobacco consumption with taxes: The Korean experience. World Bank, Washington, DC. © World Bank. <https://openknowledge.worldbank.org/handle/10986/30020> License: CC BY 3.0 IGO. "

<b>excise tax reform</b>	<p>effective tax rate. At the same time, by developing a tobacco tax rate that automatically adjusts for inflation, Korea can increase the real price of cigarettes accordingly to reflect the real purchasing power of consumers and their level of pay. Consumption trends also show that Koreans have reduced their cigarette consumption, although the reduction is not really sustainable.</p> <ul style="list-style-type: none"> <li>• Equal treatment of all cigarettes can reduce the likelihood of smokers switching their behaviour from regular cigarettes to alternative cigarettes.</li> <li>• However, the tax reform in 2015 with the sharp increase in excise tax on all tobacco products has opened the door for illegal products to the Korean market compared to the pre-reform period. Therefore, raising the excise tax too high will not be a sustainable and effective way to maintain the stability of the tobacco market, reduce tobacco consumption, and control tobacco smuggling.</li> </ul>
<b>3. Indonesia</b> <p><b>Please refer to detailed information and information sources at page number 45 - Full version of the Study on Excise Tax System.</b></p>	
<b>Overview and Status</b>	<p>Excise tax structure: specific 10 tiers tax structure and in the process of simplification (reducing the number of tiers)</p> <p><b>Excise tax policy over time:</b></p> <ul style="list-style-type: none"> <li>• 2009: Switch from ad valorem tax structure to “multi-tiered specific” tax structure. The purpose of applying a multi-tiered specific tax structure is to protect small and domestic producers from competition from large tobacco companies in the market. Tax tiering is based on production type, production capacity and retail price (with wide thresholds, specific tax rates in the range from IDR635 - IDR 985).</li> <li>• Indonesia has been raising taxes on tobacco products almost every year especially since 2014 based on its health protection policy (average of 10%-12% in each year)<sup>6</sup>. The tax increase strategy over the past 5-10 years seems to have achieved three important results as expected: (i) a significant reduction in tobacco production by 3% on average (from 320 billion to 310 billion cigarettes per year), (ii) increase of tax revenue (40-50% increase in the period 2014-2020), and (iii) cut of the youth smoking rate from 9-10% to 8.83% in the period 2020-2022<sup>7</sup>.</li> </ul>

<sup>6</sup> Government to increase excise tax on cigarettes by at least 10% by 2020<sup>6</sup> (Coconut Jakarta, 2019) and 'Indonesia to raise cigarette prices by more than a third in early 2020<sup>6</sup> (Reuters, 2019) Accessed online: February 17, 2022.

<sup>7</sup> Pursuant to Regulation No. 146/PMK.010/2017 of the Ministry of Finance

	<ul style="list-style-type: none"> <li>• However, the application of high and different tax rates at each level combined with a relatively complex tax structure (including 10 tiers) has made the price gap for cigarettes quite wide, creating opportunities for consumers switching from high-priced (higher taxed) cigarettes to cheaper products or illegal cigarettes which leads to a loss of tax revenue. The rate of illegal cigarettes is estimated at 9.7% in 2017 (falling below the 10% threshold for the first time since 2012)<sup>8</sup>. However, tax loss from the illicit tobacco trade is growing to a peak of around IDR 13.3 trillion in 2017, an increase of more than 60% compared to 2012).</li> <li>• This country is in the process of simplifying the tiers down to 8 tiers (on January 1, 2022) and the goal is to reduce them to 5 tiers.</li> </ul>
<b>Experience for Vietnam in excise tax reform</b>	<ul style="list-style-type: none"> <li>• The application of a multi-tiered specific excise tax system may be appropriate in the context of a large price gap between tobacco products, especially in the initial stage of transition from ad valorem tax structure to specific tax structure. This tax structure also helps the government to protect small and domestic producers from competition from major tobacco companies in the market, and helps to achieve the Government's goals of reducing smoking rates and increasing budget revenue.</li> <li>• However, the case of Indonesia shows that an complex tax system with too many tiers creates more administrative burdens and tends to motivate consumers to spend less on valuable brands or use cheaper alternatives, with little or no tax, which can impede the government's goal of increasing revenue and directing consumers to high-quality tobacco products thereby supporting goal of improving public health.</li> <li>• Simplifying and gradually reducing the number of tiers as well as a comfortable and consistent tax base for tobacco products will help reduce negative impacts, resulting in more predictable government revenue and effectively limit overall tobacco consumption.</li> </ul>

#### 4. The Philippines

Please refer to detailed information and information sources at page number 50 - Full version of the Study on Excise Tax System.

<b>Overview and Status</b>	<b>Excise tax structure:</b> single-tier specific tax  <b>Excise tax policy over time:</b>
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<sup>8</sup> Oxford Economics. Asia Illegal Tobacco Consumption Index 2017: Indonesia. (Accessed online February 18, 2022 from [https://illegaltobacco.oxfordeconomics.com/media/OXFO5877\\_Indonesia\\_2018\\_Report.pdf](https://illegaltobacco.oxfordeconomics.com/media/OXFO5877_Indonesia_2018_Report.pdf))

	<ul style="list-style-type: none"> <li>Period 1997 - 2012: The Philippines applied a 4-tier specific tax system. Excise tax accounted for 24.1% of average retail price and total tax expense accounted for 36.1% of average retail price. This is much lower than in countries with strict tobacco control policies, where the total cost of taxes on cigarettes accounts for more than 70% of the retail price<sup>9</sup>.</li> <li>Period 2013 - 2016: Excise tax was changed from 4-tier to 2-tier specific tax system under the 2012 tax reform (Act RA 10351 promulgated on December 20, 2012). After the reform, the proportion of excise tax per pack of cigarettes increased on average from 108% to 341%<sup>10</sup> (for low-cost brands) in 2013 and the volume of cigarettes consumed has decreased since 2012.</li> <li>From 2017 onwards: The Philippines has moved to a single-tier specific tax system. After 2017, the excise tax rate will continue to increase by 4%/year to adjust for inflation and increase by 5%/year from 2024. Budget revenue will start to increase again in 2018.</li> </ul>
<b>Experience for Vietnam in excise tax reform</b>	<ul style="list-style-type: none"> <li>The case of the Philippines shows that a gradual tax increase will gradually increase government revenue without increasing the market penetration of smuggled cigarettes.</li> <li>The Philippine experience in reforming tobacco tax structure by increasing taxes step by step over a long period and simplifying the tobacco tax structure contributes to prove that tobacco taxes are an effective policy tool in curbing smoking, expanding the fiscal space and government revenue, and providing a sustainable source of financing for health.</li> </ul>

## 5. Malaysia

**Please refer to detailed information and information sources at page number 55 - Full version of the Study on Excise Tax System.**

<b>Overview and Status</b>	<p><b>Excise tax structure:</b> single-tier specific tax</p> <p><b>Excise tax policy over time:</b></p> <ul style="list-style-type: none"> <li>During the period 2014 - 2015, Malaysia continuously increased excise tax, once in September 2015 and once in 2015 with an increase of nearly 40%. The increase in excise tax in 2015 increased the retail price of cigarettes by up to 25%. This change makes tobacco prices relatively expensive compared to</li> </ul>
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<sup>9</sup> Miguel-Baquilon, M., Luz, S., Quimbo, A., Casorla, A.A., Medalla, F.M., Xu, X., & Chaloupka, F.J. (2012). The Economy of Tobacco Products and the Tobacco Tax in the Philippines

<sup>10</sup> Jo-Ann Diosana, 'Increasing Tobacco Taxes: The Philippine Experience' (ResearchGate, 2020) <[https://www.researchgate.net/publication/342854587\\_Raising\\_Tobacco\\_Taxes\\_The\\_Philippine\\_Experience](https://www.researchgate.net/publication/342854587_Raising_Tobacco_Taxes_The_Philippine_Experience)> accessed February 5, 2022.

	<p>people's income and there is a huge gap between legal cigarettes and illegal cigarettes (legal cigarettes are about 5 times more expensive than illegal ones). As a result, Malaysian smokers switched from consuming legal products to illegal products having very low prices, around RM3/20 cigarettes. The total amount of illegal cigarettes consumed increased significantly and worsened after tax reform (65% of cigarettes consumed in 2020 are illegal products)<sup>11</sup>.</p> <ul style="list-style-type: none"> <li>As a result, the government lost revenue from excise and other taxes. The total amount of tax evaded by the illicit trade in cigarettes in 2018 was over RM5.1 billion<sup>12</sup>, which equates to nearly 3% of Malaysia's total tax collection in that year<sup>13</sup>. At the same time, the problem of illegal cigarettes has led to concerns about the health and unemployment of workers in the tobacco sector when they had to close legal tobacco factories.</li> </ul>
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<b>Experience for Vietnam in excise tax reform</b>	<ul style="list-style-type: none"> <li>The significant tax hike in Malaysia did not support the Malaysia's government to achieve their goals. Instead, it worsened the already significant problem of illicit trade and created negative domino effects in the tobacco market including continued loss of government revenue, the closure of legal tobacco factories, and loss of jobs for local workers.</li> </ul>
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## 6. The United Kingdom (the UK)

Please refer to detailed information and information sources at page number 57 - Full version of the Study on Excise Tax System.

<b>Overview and Status</b>	<p>Tax structure: Hybrid (ad valorem tax and single-tier specific tax)</p> <p><b>Excise tax policy over time:</b></p> <ul style="list-style-type: none"> <li>Tobacco prices have continued to rise in the UK since the application of a tobacco tariff adjusted to match the inflation rate (the Budget Act 2000).</li> <li>In 2011, the ad valorem rate was significantly reduced from 24% to 16.5% while the specific tax was increased to around 30% (this change raised the tax expense on cheap cigarettes).</li> <li>In 2017: Minimum excise tax (MET) policy introduced in 2017 has set the minimum level of excise tax for each pack of tobacco. It sets a price floor in</li> </ul>
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<sup>11</sup> Lee, Esther. "Revenue of 2021: Victory of the Tobacco Industry | The Edge Markets." The Edge Malaysia, November 16, 2020, <https://www.theedgemarkets.com/article/budget-2021-win-tobacco-industry>. Accessed February 7, 2022.

<sup>12</sup> isentia. 2019. "The highest illegal tobacco use in the world." Malaysia SME, (July).

[https://www.batmalaysia.com/group/sites/BAT\\_AP6D2L.nsf/vwPagesWebLive/DOBXHDEA/\\$FILE/Malaysia\\_has\\_world's\\_highest\\_incidence\\_of\\_illegal\\_tobacco\\_use-Malaysia\\_SME.pdf?openElement](https://www.batmalaysia.com/group/sites/BAT_AP6D2L.nsf/vwPagesWebLive/DOBXHDEA/$FILE/Malaysia_has_world's_highest_incidence_of_illegal_tobacco_use-Malaysia_SME.pdf?openElement).

<sup>13</sup> Oxford Economics. 2019. "The ECONOMY OF ILLEGAL TOKYO EXCHANGE IN MALAYSIA." *TOBACCO INDUSTRY REPORT IN UK*, (June).

	<p>both specific tax and ad valorem tax components.</p> <ul style="list-style-type: none"> <li>• The implementation of a tobacco tax increase and the introduction of a minimum excise tax (MET) resulted in a very high tax burden and made smoking extremely expensive (currently tobacco taxes are around £5.26 /pack of 20 cigarettes, plus 16.5% on retail price and VAT). As a result, legal cigarette consumption has declined steadily from 49.5 billion cigarettes in 2005-06 to only around 29.5 billion cigarettes in 2016-17<sup>14</sup>.</li> <li>• However, the above-mentioned excessively high tobacco tax policy has boosted the market for consumption of illegal cigarettes and counterfeit cigarettes. The illegal tobacco trade has become a prominent problem in the UK (about 20% market share). This leads to an increased risk of harm to health<sup>15</sup> as well as a loss of tax revenue (estimated at around £2.3-2.5 billion between 2016-17 and 2019-20<sup>16</sup>). Along with that, the employment rate in the retail industry has been seriously reduced (reducing from 6,640 to 11,190 jobs)<sup>17</sup>.</li> </ul>
<b>Experience for Vietnam in excise tax reform</b>	<ul style="list-style-type: none"> <li>• The UK represents one of the countries with the hybrid tobacco taxation system where the authority is committed to maintaining high tobacco tax rates to mainly discourage consumption.</li> <li>• Although some health goals have been achieved by reducing consumption, the application of this tax policy also has disadvantages such as negative impact on state budget revenues due to changes in consumer choices from legal products to illicit cigarettes which have gradually normalized over time. 'Smuggling' is also gradually becoming a prominent problem when large-scale organized crime and complex distribution networks penetrate deep and wide into the country.</li> </ul>

<sup>14</sup> Annex 3 - UK

<sup>15</sup> Rodrigo, 'History of UK tobacco tax policy and related consequences?' (Writepass Journal, 2016) Accessed February 10, 2022.

<sup>16</sup> 'Measuring Tax Disparities - 2017 edition: Estimated Tobacco Tax Disparities for 2016-2017' (HMRC, 2017) Accessed online: February 10, 2022.

<sup>17</sup> Oxford Economics, 2016, Effect of drug pack size on retail spending