

FCTC Evaluation

Sri Lanka's compliance with Article 6:

Price and tax measures to
reduce the demand for tobacco

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1

Introduction

Tobacco use is currently the leading cause of preventable death, having claimed over 50 million lives in the past decade (World Health Organisation, 2015). The health consequences of tobacco place a heavy economic burden on countries through decreased labour productivity and increased healthcare costs. The World Health Organisation (WHO) actively advocated the reduction of worldwide tobacco consumption by adopting the Framework Convention of Tobacco Control (FCTC) in 2003. The FCTC binds signatory countries to employ functional methods of regulating tobacco use, including the implementation of tax and price measures on tobacco products.

Sri Lanka has always maintained a political and social interest in tobacco control. The country ratified the Framework in 2003 and introduced tobacco control legislation through the National Authority on Tobacco and Alcohol Act, No 27 of 2006 (NATA Act). This legislation included several regulations in line with the FCTC recommendations such as banning the free distribution and advertising of tobacco products. Despite making progress, Sri Lanka has yet to implement several other recommendations of the FCTC, especially with regard to tobacco taxation and pricing as outlined in Article 6 of the FCTC. As a signatory, Sri Lanka is obligated to follow the FCTC's recommendations to reduce tobacco demand.

This briefing note evaluates Sri Lanka's compliance with Article 6 of the FCTC through its existing policies on tobacco control. Section 2 of the briefing note provides an overview to Article 6 of the FCTC and its recommendations. It also describes the methodology employed to evaluate Sri Lanka's compliance with the recommendations. Section 3 evaluates each recommendation by category to assess its impact on better tax and price outcomes as well as Sri Lanka's current compliance for both cigarettes and other tobacco products (OTPs). In Section 4, the findings are analysed at the category, product and recommendation levels. Section 5 concludes with several interventions to improve compliance with FCTC Article 6.

2

Background

2.1. Overview

The Framework Convention on Tobacco Control (FCTC) is the world's first public health treaty and was adopted by the WHO in 2003 at the 56th World Health Assembly.¹ At present, the treaty has 168 signatories and 180 parties. The FCTC is divided into nine parts, which outline the recommendations and best practices in key areas for tobacco control. The FCTC includes measures for reducing demand and supply of tobacco.

Part III of the Framework focuses on measures for reducing the demand for tobacco. Article 6 under Part III highlights the importance of one such measure, tobacco taxation and pricing. Article 6 reads as follows:

- 1.** The Parties recognise that price and tax measures are an effective and important means of reducing tobacco consumption by various segments of the population, in particular young persons.
- 2.** Without prejudice to the sovereign right of the Parties to determine and establish their taxation policies, each Party should take account of its national health objectives concerning tobacco control and adopt or maintain, as appropriate, measures which may include:
 - a.** implementing tax policies and, where appropriate, price policies, on tobacco products so as to contribute to the health objectives aimed at reducing tobacco consumption; and
 - b.** prohibiting or restricting, as appropriate, sales to and/or importations by international travellers of tax- and duty-free tobacco products.

1. The World Health Assembly is the policymaking body of the WHO, which is attended by all WHO member states. It is held annually at Geneva, Switzerland.

3. The Parties shall provide rates of taxation for tobacco products and trends in tobacco consumption in their periodic reports to the Conference of the Parties, in accordance with Article 21.

As stated in Section 2 of Article 6, the Convention does not dictate tax policies to Parties, but rather urges them to amend their tobacco-related policies to increase prices and taxes and thereby reduce affordability of tobacco products, thereby reducing consumption and achieving public health objectives. An additional benefit of such tax and price increases, which is not explicitly mentioned in Article 6, is its contribution to government revenue.

In order to assist parties in implementing the measures in Article 6, the WHO published the *Guidelines for Implementation of Article 6*, which was adopted by the Conference of the Parties at its sixth session (decision FCTC/COP6(5)). This document draws on available evidence, best practices, and the experience of the Parties that have successfully reduced tobacco consumption through tax and price measures. It identifies six guiding principles that underpin the implementation of Article 6:

- i. Determining tobacco taxation policies is a sovereign right of the Parties.
- ii. Effective tobacco taxes significantly reduce tobacco consumption and prevalence.
- iii. Effective tobacco taxes are an important source of revenue.
- iv. Tobacco taxes are economically efficient and reduce health inequalities.
- v. Tobacco tax systems and administration should be efficient and effective.
- vi. Tobacco tax policies should be protected from vested interests.

Based on these principles, the Guidelines makes actionable recommendations for implementing Article 6.

2.2. Methodology

The purpose of this briefing note is to evaluate Sri Lanka's level of compliance with the FCTC recommendations for tax and price measures under Article 6. Five categories of guidelines were selected from the *Guidelines for Implementation of Article 6*, and 19 recommendations were identified for assessment (see Box 1).

BOX 1

Category 1: Relationship between tobacco taxes, price and public health

- ❖ Recommendation 1.1: Have regular adjustment processes or procedures for periodic revaluation of tobacco tax levels
- ❖ Recommendation 1.2: Take into account price elasticity and income elasticity of demand, inflation and changes in household income when establishing or increasing taxes

Category 2: Tobacco taxation systems

- ❖ Recommendation 2.1: Implement a specific or mixed/hybrid tax system
- ❖ Recommendation 2.2: Establish coherent long-term policies on tobacco taxation structure
- ❖ Recommendation 2.3: Monitor tax rates on a regular basis
- ❖ Recommendation 2.4: Tax all tobacco products in a comparable way

Category 3: Tax administration

- ❖ Recommendation 3.1: Ensure that transparent license or equivalent approval and control systems are in place
- ❖ Recommendation 3.2: Adopt and implement measures and systems of storage and production warehouses to facilitate excise controls on tobacco products
- ❖ Recommendation 3.3: Impose excise taxes at the point of manufacture, importation, or release for consumption from the storage or production warehouses to reduce the complexity of tax collection systems
- ❖ Recommendation 3.4: Require by law that tax payments are remitted at fixed intervals or on a fixed date each month
- ❖ Recommendation 3.5: Report production and/or sales volumes, and price by brands, taxes due and paid, and volumes of raw material inputs
- ❖ Recommendation 3.6: Mandate tax authorities to allow for the public disclosure of the information in reports
- ❖ Recommendation 3.7: Impose effective anti-forestalling measures, in anticipation of tax increases
- ❖ Recommendation 3.8: Require application of fiscal markings
- ❖ Recommendation 3.9: Clearly designate and grant appropriate powers to tax enforcement authorities
- ❖ Recommendation 3.10: Provide for information sharing among enforcement agencies in accordance with national law
- ❖ Recommendation 3.11: Provide for an appropriate range of penalties to deter non-compliance with tax laws

Category 4: Use of revenues - financing of tobacco control

- ❖ Recommendation 4.1: Dedicate revenue to tobacco control programs

Category 5: Tax-free/ duty-free sales

- ❖ Recommendation 5.1: Prohibit or restrict the sale to and importation by international travellers, of tax-free/ duty-free tobacco products

Source: Adopted from the Guidelines for Implementation of Article 6, WHO FCTC.

The evaluation of the WHO FCTC Article 6 is done by first scoring the significance of each recommendation (impact score), and then scoring the extent to which Sri Lanka has adopted the recommendations (compliance score).

Impact Score

The impact score evaluates each recommendation based on (a) its impact on tobacco demand reduction and (b) the timeframe required for implementation. The intuition behind this method is to assist with setting priorities for policy action. That is, those recommendations with a high impact and those that can be implemented quickly should be prioritized over those with a low impact and those that need more time for implementation. Therefore, the impact score of each recommendation is assessed on a scale of 1-4 as follows:

High impact (score of 3.5, 4): recommendations have a strong direct influence on reducing tobacco consumption through either tax or price of tobacco products and require immediate action (within one year) to ensure sound tobacco control.

Medium impact (score of 2, 2.5): recommendations have a direct impact on information disclosure, which will lead to better tobacco control through greater transparency and/or recommendations that can be incorporated in the medium term (within one to three years).

Low impact (score of 1): recommendations require a re-allocation of current resources and/or have little direct impact on the tobacco consumer and can be considered in the long term (between three to five years).

The assessment of the score is based on an evaluative judgement made by the researchers. In assigning a score, the researchers have attempted to reflect an ordinal scale.

Compliance Score

The compliance score evaluates each recommendation on the level at which (a) legislation, (b) policy, (c) actions and (d) the surrounding discourse are consistent with complying with the recommendation in Sri Lanka. Its evaluation is based on the provisions of three Acts: Excise (Special Provisions) Act, No. 13 of 1989; Tobacco Tax Act, No. 8 of 1999; and National Authority on Tobacco Control Act, No. 27 of 2006.

Discourse is included in the compliance scoring because while legislation is the strongest means of compliance, a discourse on the principles and issues helps to ensure that appropriate policies and actions follow the legislation. Even when there are no actions, policies, or legislation, a discourse advocating action is a starting point for bringing about the movement needed in these areas.

Compliance with the recommendations is scored on a scale of 0-10 as follows:

Strong compliance (score of 7.6-10): the recommendation is currently incorporated in national legislation or policy and is currently functional and in practice.

Moderate compliance (score of 4.6-7.5): the recommendation is largely functional or incorporated in national legislation or policy and there is significant public discourse towards the implementation of the recommendation.

Poor compliance (score of 1.5-4.5): the recommendation is only partially incorporated in national legislation or policy, and public discourse towards the implementation of the recommendation is weak.

No compliance (score of 0-1.4): none of the components of the recommendation are functional or incorporated in national legislation or policy, and public discourse towards implementation is little to none.

Compliance is also scored through an evaluative judgement made by the researchers using an approximately ordinal scale from 0 to 10, with zero representing no compliance (where there is neither a plan nor discussion on compliance).

Sri Lanka's tobacco control laws focus largely on cigarettes, which have the largest market share of all tobacco products. Cigarettes are manufactured and distributed by a monopoly Ceylon Tobacco Company (CTC), in sharp contrast to the manufacture of other tobacco products in the market, which is both informal and decentralized. Therefore, when assessing compliance with each recommendation, a distinction will be drawn between cigarettes and other tobacco products (OTPs). The latter includes smoked tobacco products, such as beedi and cigars, and non-smoked tobacco products, such as betel quid and babul.

3

Evaluation of FCTC Article 6 on impact and compliance

3.1. Summary of Sri Lanka's compliance with Article 6

Of the 19 actionable recommendations made in the *Guidelines to the Implementation of Article 6*, six have a high impact score (31.6%), ten have a medium impact score (47.3%) and three have a low impact score (21.1%).

The average compliance score (out of 10) varies for the different levels of impact (see Table 1 and Figure 1). The overall impact-weighted average compliance score is 6.3 for cigarettes (indicating moderate compliance) and 3.6 for other tobacco products (indicating poor compliance).²

Table 1: Average compliance with FCTC recommendations categorised on impact level

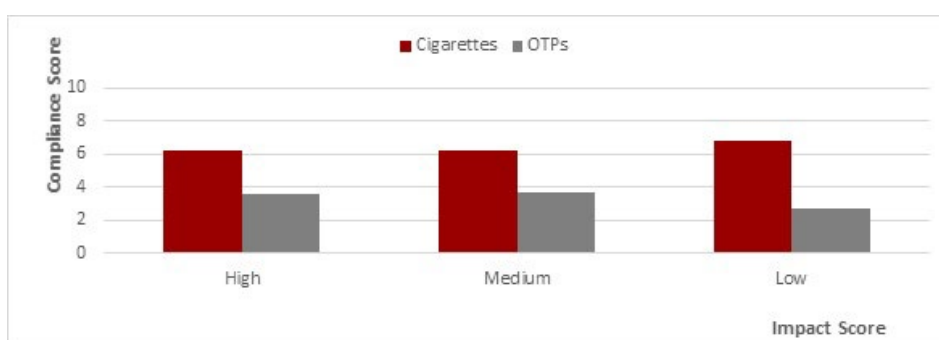
Impact	Average compliance score	
	Cigarettes	OTPs
High (3.5, 4.0)	6.2	3.6
Medium (2.0, 2.5)	6.2	3.7
Low (1.0)	6.8	2.7

2. In weighting the compliance score by impact, the compliance score for a recommendation with a high impact score gets a proportionally higher weight than the same compliance score for a recommendation that has a low impact score. This provides an overall impact adjusted assessment of compliance to the FCTC recommendations.

Impact	Average compliance score	
	Cigarettes	OTPs
Overall score (impact-weighted average compliance score of all the recommendations)	6.3	3.6

Source: Author's calculation based on the FCTC Evaluation.

Figure 1: Average compliance with FCTC recommendations categorised by impact



Source: Author's calculation based on the FCTC Evaluation.

For cigarettes, compliance is highest with recommendations that have a low impact on tobacco consumption and control. For OTPs, compliance is lowest at this impact level and higher for high and medium impact level recommendations at 3.6-3.7. However, even at those impact levels, compliance scores for OTPs fall short of cigarettes by 2.6-2.5. Generally, compliance has been higher for cigarettes than for OTPs with the impact-weighted compliance scores moderate (at 6.3) and poor (at 3.6) respectively.

3.2. Category 1: Relationship between tobacco taxes, prices and public health

Category 1 relates to the effective use of taxation and pricing to reduce both consumption and prevalence of tobacco products. In most cases, higher taxes on tobacco products lead to higher prices, which in turn lead to lower consumption and prevalence, resulting in a reduction of mortality and morbidity in the population.

There are two actionable recommendations under this category. Overall, the recommendations in Category 1 have high impact scores, with an moderate average compliance score for cigarettes and an poor average compliance score for OTPs. Table 2 gives the impact and compliance scores of each recommendation.

Table 2: Evaluation of recommendations under Category 1

Recommendation	Impact	Compliance	
		Cigarettes	OTPs
1. Relationship between tobacco taxes, prices, and public health			
1.1 Have regular adjustment processes or procedures for periodic revaluation of tobacco tax levels	High (4)	Moderate (6)	Poor (2)
1.2 Take into account price elasticity, income elasticity of demand, inflation and changes in household income when establishing or increasing taxes	High (4)	Moderate (5)	No compliance (1)
Average	High (4)	Moderate (5.5)	Poor (1.5)

Recommendation 1.1: Have regular adjustment processes or procedures for periodic revaluation of tobacco tax levels

Impact

Recommendation 1.1 has a high impact score since taxation and pricing have a direct and rapid impact on tobacco demand. Without regular tax (and thereby price) adjustments, the real prices of tobacco products erode with inflation and household income growth.³ As regular tax adjustments maintain or reduce the affordability of tobacco products by influencing price, their impact on reducing tobacco consumption is high.

Compliance

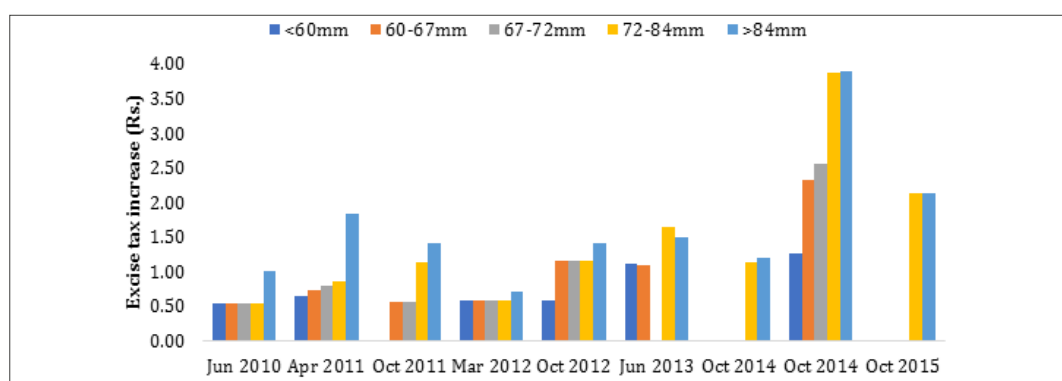
Sri Lanka's tobacco regulations do not mandate frequent adjustments of taxation. However, the National Authority on Tobacco and Alcohol (NATA) has actively lobbied for regular adjustments of taxes on tobacco products as part of their mandate in advising, monitoring, evaluating, and recommending policies aimed at reducing tobacco consumption.⁴

On cigarettes, excise taxes were amended at least once a year during 2010-2015. However, the annual amendments were applied unevenly across the length-based tariff bands. For example, the excise taxes on cigarettes 72-84 mm in length (which accounted for 87% of consumption in 2015) were amended nine times between 2010 and 2015, whereas the excise taxes on cigarettes of less than 60mm in length—the band length with the second largest market share—were only adjusted six times (Figure 2).

However, cigarettes are evaluated as having a moderate compliance score since there has been periodic, albeit sporadic, revisions of cigarette excise taxes, and agencies (including NATA) have persistently lobbied in favour of regular tax amendments.

3. The tax component affected are specific taxes.

4. This agency was empowered under the National Authority on Tobacco and Alcohol Act, No. 27 of 2006.

Figure 2: Cigarette excise tax increases (2010-2015)

Source: Calculated by tax rates published in gazettes under Excise (Special Provisions) Act, No. 13 of 1989.

Tax adjustments for OTPs are more irregular than for cigarettes; selected smoked tobacco products—such as cigars, cheroots, and cigarillos—are subject to taxes which were only amended once in the period 2010–2015. In addition, beedi and smokeless tobacco products, which are mainly produced by the informal sector, are not subject to any direct taxes. Therefore, Recommendation 1.1 is evaluated as having a poor compliance score for OTPs.

Overall Recommendation 1.1 is evaluated at a moderate compliance score for cigarettes and a poor compliance score for OTPs.

Recommendation 1.2: Take into account price elasticity, income elasticity of demand, inflation and changes in household income when establishing or increasing taxes

Impact

Recommendation 1.2 is assessed as having a high impact score. Over time, increases in household income and inflation make tobacco products more affordable both in real and relative terms. For tax changes and subsequent price increases to have an impact on reducing consumption, they should make tobacco products less affordable. Therefore, tobacco tax adjustments can be more precisely calibrated to achieve the desired consumption and prevalence levels by taking into consideration household income changes and inflation (including the application of income and price elasticities).

Compliance

Cigarette tax revisions have failed to reduce the affordability of the tobacco product; according to de Mel and Fernando (2015), nominal cigarette price increases in Sri Lanka have kept pace with nominal income (measured in terms of per capita GDP terms) during 1980–2000, but thereafter the price increases failed to keep-up and cigarettes have become more affordable (see Figure 3).⁵ It must be noted, however, by coincidence and not conscious design, cigarette tax increases have outpaced inflation.⁶

5. de Mel & Fernando (2015) evaluated the changes in price of the most sold brand of cigarettes in Sri Lanka - John Player Gold Leaf (JPGL) with 87% of the market in 2015 - against changes in per capita GDP.

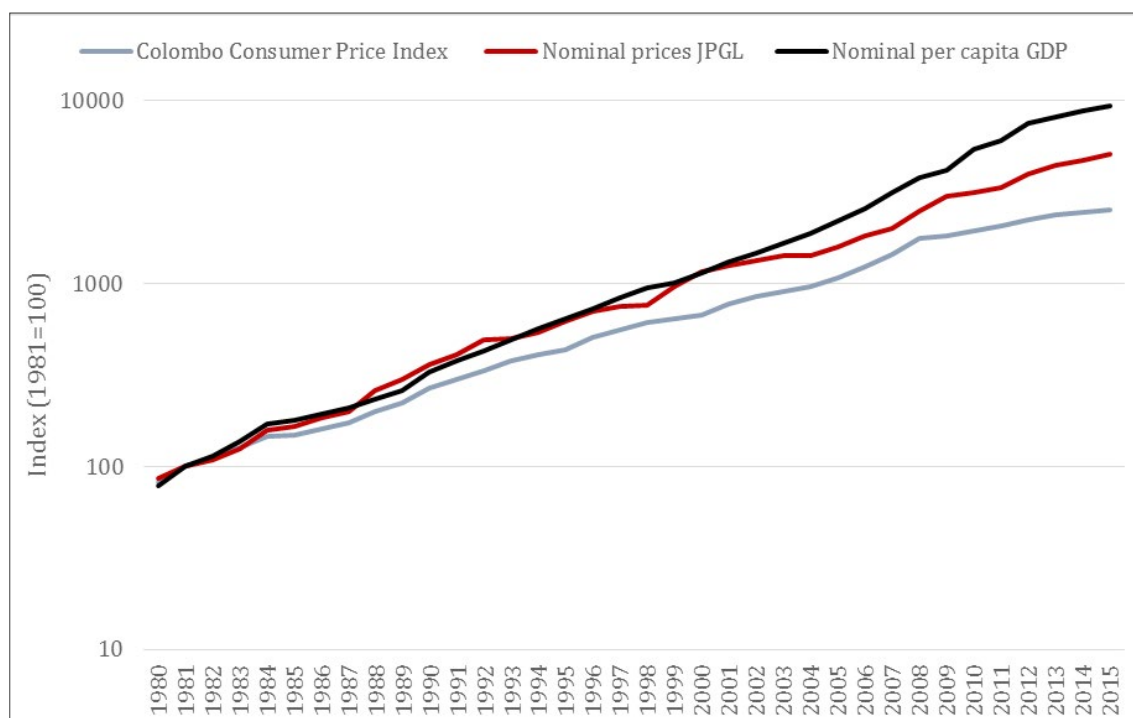
6. Adapting the methodology of de Mel and Fernando (2015), Figure 3 shows that adjustments in cigarette prices have consistently outpaced inflation (measured by the movements of the Colombo Consumer Price Index (CCPI)) since 1980.

However, there are weaknesses in accounting for elasticities of income and of price related to tobacco consumption. These calculations require regular national level consumer surveys to track cigarette consumption patterns and behaviour. Sri Lanka currently does not generate this data, and therefore, does not have the capacity to implement this aspect of the recommendation. Nevertheless, there are global studies that have been undertaken, including for developing nations, which have estimated the relationship between price, income, and consumption of cigarettes to a reasonable degree. Although NATA has recommended to the government to adopt a tax formula based on these estimates, policymakers still fail to use tools such as these when deciding cigarette excise rates. Taking all the above into account the Recommendation 1.2 is evaluated to have a moderate compliance score on cigarettes.

At present, tobacco tax amendments in Sri Lanka do not aim to reduce cigarette and OTP affordability by considering income growth, inflation, and income and price elasticities. The relative lack of tax revisions for OTPs relative to cigarettes, however, means that compliance for OTPs is worse than cigarettes. Not only are they more irregularly and inconsistently taxed, the informal nature of manufacture and retail of OTPs makes it difficult to track price changes over time and assess affordability (i.e., income and inflation) and consumer behaviour (i.e., elasticities of price and income). As such, Recommendation 1.2 for OTP is evaluated to have no compliance.

Overall Recommendation 1.2 is evaluated as demonstrating a moderate compliance score for cigarettes and a score of no compliance for OTPs.

Figure 3: Movements of nominal JPGL prices, per capita nominal income and CCPI indexes (1981 =100)



Source: Author's calculations based on data from Annual Report, Central Bank of Sri Lanka (multiple years).

3.3. Category 2: Tobacco taxation systems

Category 2 considers long-term policies for revisions in tobacco tax structure, including mechanisms for monitoring. The recommendations under this category are aimed at achieving the objectives of tobacco policy as outlined in Category 1 in a systematic way.

The four actionable recommendations under this category relate to improving the tobacco tax system. Overall, the recommendations in Category 2 have been evaluated as having on average a high impact score, and an average compliance score that is moderate for cigarettes and poor for OTPs (Table 3).

Table 3: Evaluation of recommendations under Category 2

Recommendation	Impact	Compliance	
		Cigarettes	OTPs
2. Tobacco taxation systems			
2.1 Implement a specific or mixed/hybrid tax system	High (4)	Strong (10)	Moderate (5)
2.2 Establish coherent long-term policies on tobacco taxation structure	High (3.5)	Poor (4)	Poor (4)
2.3 Monitor tax rates on a regular basis	Medium (3.5)	Poor (4)	Poor (2)
2.4 Tax all tobacco products in a comparable way	High (3.5)	Poor (4)	Poor (2)
Average	High (3.4)	Moderate (5.5)	Poor (3.3)

Recommendation 2.1: Implement a specific or mixed/hybrid tax system

Impact

Recommendation 2.1 is assessed as having a high impact score. Of the tax options for tobacco products, the FCTC recommends a specific tax system, or a mixed/hybrid tax system with a minimum specific tax floor. A greater reliance on the specific excise tax component reduces the gap in price between premium and low-priced tobacco products, thereby limiting possible substitution to cheaper alternatives in response to tax increases (WHO, 2010).⁷ Other merits of specific taxes are that they are easy to apply and administer and less dependent on industry pricing strategies, while generating revenue that is relatively predictable. Hence, the tax structure is an important factor in regulating the price and profitability of tobacco products, and the adherence to Recommendation 2.1 improves policymakers' capacity for tobacco control.

7. The FCTC recognises three primary types of taxes: specific, ad valorem and mixed/hybrid. Specific taxes are those that do not change based on product price but are a fixed amount per unit of the product. Ad valorem taxes are taxes that are applied as a percentage, often based on the price of a product. Mixed/hybrid taxes include both specific and ad valorem tax components; this would involve a specific tax that is fixed per unit of the product along with an ad valorem tax that varies with the price per unit.

Compliance

Sri Lanka currently has a specific tax structure for cigarette excise taxes, which is applied based on cigarette length. There are five length bands, though locally manufactured cigarettes fall into only four of these categories (Table 4). Compliance of cigarettes with Recommendation 2.1 is evaluated as strong because the FCTC best practices of using specific excise taxes is currently the practice in Sri Lanka.

In contrast, the tax structure for OTPs, is deficient. On the one hand, while some smoked tobacco products—i.e., cigars, cheroots and cigarillos and piped tobacco—have a specific excise tax implemented under the Tobacco Tax Act, No. 8 of 1999, this tax has been fixed at LKR 10 per kilogram of tobacco for almost two decades. On the other hand, more informally produced OTPs are not directly taxed at production or retail stages but may be subject to border taxes if any of the raw materials are imported.⁸ Hence, as the taxes on OTPs have either been static for a long period of time or indirectly taxed if they exist, their compliance with Recommendation 2.1 is evaluated as moderate.

Overall Recommendation 2.1 is evaluated as having a strong compliance score for cigarettes and a moderate compliance score for OTPs.

Table 4: Excise duty and cigarette brands as at August 2016⁹

Length category	Excise duty per cigarette (LKR)	Cigarette brands
Cigarettes not exceeding 60mm	6.975	Capstan Plain, Three Roses
Cigarettes exceeding 60mm but not exceeding 67mm	12.675	Four Aces
Cigarettes exceeding 67mm but not exceeding 72mm	14.660	Bristol
Cigarettes exceeding 72mm but not exceeding 84mm	23.750	John Player Gold Leaf, Dunhill
Cigarettes exceeding 84mm	27.240	N/A

Source: Handbook of Drug Information 2014, National Dangerous Drugs Control Board; Gazette No. 1934/40 – Friday, October 02, 2015.

8. For example, the tendu leaf, which forms the wrapping of the beedi stick is imported from India under a customs duty of LKR 2,000 per kilogram (or 25-50% of retail price). In addition to these specific taxes, ad valorem taxes such as Value Added Tax (VAT), Nation Building Tax (NBT), Port and Airport Levy (PAL) and Import Cess are charged on imports, creating a hybrid tax system.
9. Actual data on the effective length bands for 2016 is published in the Handbook of Drug Abuse Information 2017, published by the National Dangerous Drugs Control Board. However, as this publication was unavailable at the time this report was published, information from the Handbook of Drug Information 2014 was used as an estimate for 2016.

Recommendation 2.2: Establish coherent long-term policies on tobacco taxation structure

Impact

Recommendation 2.2 is assessed as having a high impact score. Several studies modelling tobacco use have found that demand is more responsive to price in the long run than it is in the short run (WHO, 2010). As such, if national taxation policies are to achieve public health objectives, they need to be designed and implemented for the long term. In addition, the existence of coherent policies underpins the success of a number of other high impact recommendations on tax and price measures.

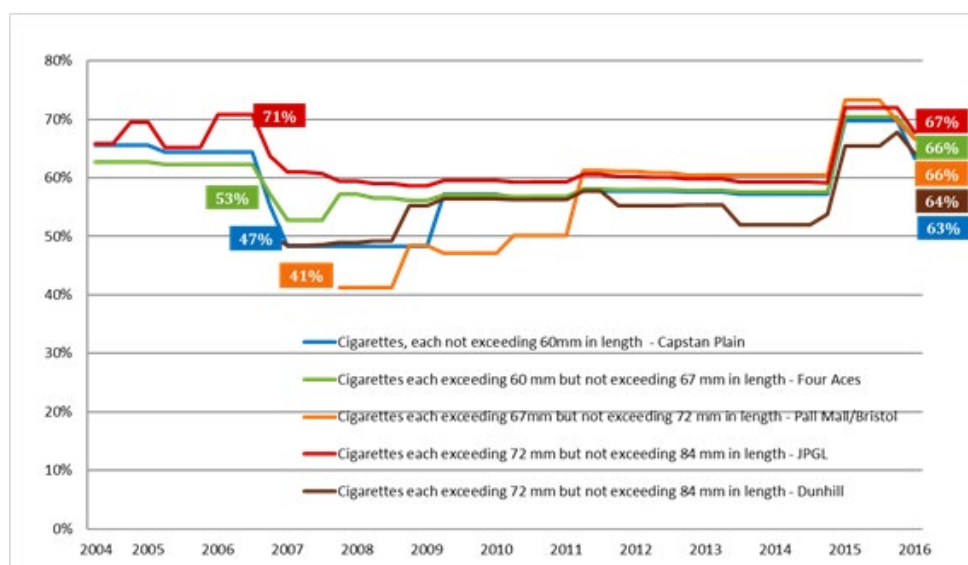
Compliance

To date, Sri Lanka has not formalised its long-term objectives or policies with regard to tobacco taxation, despite much political and public anti-tobacco sentiment. The regulations governing the taxation of tobacco products in the last decade, for instance, was not based on a long-term policy or stated long-term policy objectives.

The evidence for the lack of long-term policies for tobacco is demonstrated through two observations of the most consistently taxed tobacco product – cigarettes. First, the cigarette tax increase since 2000 has fallen short of income increase, making cigarettes more affordable over time (Figure 3). Second, the variation in tax rates between cigarette length bands has persisted over time, as seen in Figure 4.¹⁰ However, there has been positive public discourse on the need for greater tobacco control and a coherent tobacco tax policy, which has been echoed by numerous stakeholders, including NATA.

Overall, Recommendation 2.2 is evaluated as demonstrating a poor compliance score for both cigarettes and OTPs.

Figure 4: Tax rate changes (2004-August 2016)



10. During the last decade, the largest gap between cigarette bands was in 2008 where cigarettes between 67-72mm had an excise tax rate of 41% whereas 72-84mm cigarettes were charged 60%.

Note: The sharp increase in 2015 offsets the removal of VAT (12%) and NBT (2%) from cigarettes during the period. Total taxes were therefore not increased, even though the excise taxes were.

Source: Calculation based on cigarette prices and excise taxes based on government gazettes.

Recommendation 2.3: Monitor tax rates on a regular basis

Impact

Recommendation 2.3 is assessed as having a medium impact score. Monitoring tax rates yields information about tobacco taxes that enable regular adjustment. Such adjustment is essential as the real value of specific taxes erodes over time due to inflation and income increases (see Recommendation 1.2). Monitoring, however, is only the first step of adjustment—a necessary but insufficient action.

Compliance

Monitoring requires the documentation of both tax rates and prices of products as these vary by product, brand, and over time. While some information on taxes and prices is available through informal channels and ad hoc reports by NATA, no single body has been officially assigned the responsibility of monitoring and publishing this data. The regulatory authorities involved in the taxation of tobacco products (i.e. Ministry of Finance, Department of Customs, and Department of Excise) do not publish periodical review and reports on tax rates and prices. The unavailability of data from the enforcement agencies involved in tobacco control also makes it apparent that there is weak, if any, monitoring mechanism in place to track tax rates.

Figure 4 shows the knock-on impact of poor monitoring. While specific excise taxes (in absolute terms) have risen over the years, these rates have large discrepancies that could have been avoided with clear monitoring structures, including provision of public information on the impact of changes in tax rates. NATA has conducted sporadic reviews via third parties; however, there is no institutionalised process for monitoring. Hence, compliance with Recommendation 2.3 is classified as poor for cigarettes.

For OTPs, compliance with Recommendation 2.3 is classified as poor at a lower score than for cigarettes, as data sources are even more deficient for the purpose of monitoring taxes and prices. Only the quantity of beedi can be estimated using the import of the key ingredient (tendu leaves) as a proxy measure, under the assumption that all beedi leaves are imported. There are no similar or reliable production estimates for other OTPs. The lack of data will be further addressed in Category 3.

Overall Recommendation 2.3 is evaluated at having poor compliance scores on both cigarettes and OTPs.

Recommendation 2.4: Tax all tobacco products in a comparable way

Impact

Recommendation 2.4 is assessed as having a high impact score. Worsening of price differentials after tax increases, especially between same type of tobacco product (such as between different cigarette

brands), can result in users switching to cheaper substitutes. As such, the FCTC recommends a harmonised tax structure for all types of tobacco products to avoid price differentials and achieve more effective taxation.

Compliance

Excise taxes effectively fall within four categories depending on the length with filter of the cigarette (there are no cigarettes in the market longer than 84 mm)¹¹. As Figure 5 shows, excise tax increases in the last five years have been uneven across the length categories: for instance, from late 2012 to 2014, excise tax increases of cigarettes that are longer than 72 mm have increased at significantly higher rates than other cigarette length categories, highlighting the concerns of inconsistency.

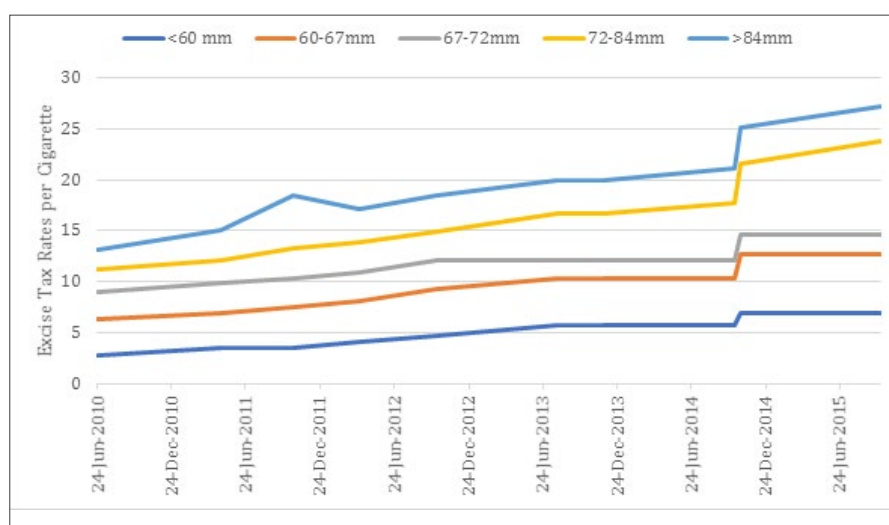
The tax variance has resulted in increasing the price differential between various cigarette lengths. When the most expensive cigarette brand (Dunhill Switch) was first introduced to the market in 2014, it was priced at 3.5 times the cheapest brand (Capstan). Subsequently, when the price of the most expensive brand was increased (Dunhill Switch at LKR 38) in October 2015, the price of cheapest cigarette stayed unchanged (Capstan at 10), resulting in the former being priced at 3.8 times the latter. This assessment shows that compliance with Recommendation 2.4 is poor for cigarettes.

There is great variation in the method of taxation between different tobacco products. Cigarettes are taxed on production, while beedi is taxed indirectly via taxes on the import of the tendu leaf. Additionally, the effective tax-to-price ratio applied to cigarettes is significantly higher than to beedi, resulting in the latter being priced much lower than the former; the cheapest cigarette in the market, for instance, is 3.6 times more expensive than a typical beedi stick. Smokeless tobacco products, such as betel quid, are not subject to any taxes. Hence, as the differences in method and percentage of taxation have created significant price variance between tobacco products. As such, Sri Lanka's compliance with Recommendation 2.4 is assessed as being poor for OTPs as well.

The need for stronger taxation and regulation on OTPs such as beedi and smokeless tobacco products has been highlighted in NATA's most recent policy recommendation to the Cabinet of Ministers. There are indications that the importance of comparable taxation has been recognised by policy advisors, even if not put into effect, as at present.

Overall, Recommendation 2.4 is evaluated as demonstrating poor compliance for both cigarettes and OTPs.

11. Presently, Capstan is the sole unfiltered cigarette in the market.

Figure 5: Cigarette excise tax amendments based on length band


Source: Gazettes published under Excise (Special Provisions) Act, No. 13 of 1989.

3.4. Category 3: Tax administration

Effective tax administration is an important aspect of tobacco control as it ensures high compliance by taxpayers, and has a low cost compared to the revenue it generates (WHO, 2010). There are 11 actionable recommendations under this category that deal with licensing, storage and warehousing, basis of taxation and disclosure of information (Table 5).

Overall, the recommendations in Category 3 have been evaluated as having a medium impact score, and a weighted average compliance score that is moderate for cigarettes and poor for OTPs. The evaluated impact and compliance score of each recommendation is summarised in Table 5.

Table 5: Evaluation of recommendations under Category 3

Recommendation	Impact	Compliance	
		Cigarettes	OTPs
3. Tax administration			
3.1 Ensure that transparent license or equivalent approval and control systems are in place	Low (1)	Strong (9)	Poor (3)
3.2 Adopt and implement measures and systems of storage and production warehouses to facilitate excise controls on tobacco products	Low (1)	Strong (8)	N/A

Recommendation	Impact	Compliance	
		Cigarettes	OTPs
3. Tax administration			
3.3 Impose excise taxes at the point of manufacture, importation, or release for consumption from the storage or production warehouses to reduce the complexity of tax collection systems	Medium (2)	Strong (9)	Moderate (5)
3.4 Require by law that tax payments are remitted at fixed intervals or on a fixed date each month	Medium (2)	Strong (10)	N/A
3.5 3.5 Report production and/or sales volumes, and price by brands, taxes due and paid, and volumes of raw material inputs	Medium (2.5)	Strong (9)	Poor (2)
3.6 Mandate tax authorities to allow for the public disclosure of the information in reports	Medium (2.5)	Moderate (7)	Moderate (7)
3.7 Impose effective anti-forestalling measures, in anticipation of tax increases	Medium (2.5)	No compliance (1)	No compliance (1)
3.8 Require application of fiscal markings	Medium (2)	No compliance (0)	No compliance (0)
3.9 Clearly designate and grant appropriate powers to tax enforcement authorities	Medium (2)	Strong (9)	Poor (4)
3.10 Provide for information sharing among enforcement agencies in accordance with national law	Medium (2)	Strong (9)	Strong (9)
3.11 Provide for an appropriate range of penalties to deter non-compliance with tax laws	Medium (2.5)	Moderate (7)	Moderate (7)
Average	Medium (2)	Moderate (7.1)	Poor (4.1)

Recommendation 3.1: Ensure that transparent license or equivalent approval and control systems are in place

Impact

Recommendation 3.1 is assessed as having a low impact score. The outcomes of this recommendation contribute to tobacco control by addressing supply-side issues (such as illicit trade) that do not have a direct effect on tobacco consumption.

Licensing and equivalent approval or control systems are a best practice in tobacco tax administration since they strengthen the capacity of the relevant authorities to monitor the tobacco product market and identify and penalise tax evasion (WHO, 2010). However, the impact of this recommendation in Sri Lanka is low. On the one hand, cigarettes have a monopoly producer. OTPs, on the other hand, are manufactured by informal cottage industries, making licensing difficult and requiring the

regulatory authorities to have dedicated physical and human resources.

Compliance

The manufacturing, storing, importing or exporting of any raw materials or finished products of cigarettes requires the certification of registration by the Commissioner General of Excise according to the Tobacco Tax Act, No. 8 of 1999 (Figure 6). Additionally, cigarette vendors, who form an important part of the tobacco supply value chain, require registration and licensing. Hence, regarding cigarettes, Sri Lanka has high compliance with Recommendation 3.1.

Figure 6: Mandated licence and registration

Date : _____.	_____ Signature of Applicant.
* When applying for certificate of registration for manufacture of beedi and cigars plan of the premises specified under item 7 of Schedule I is not required.	
SCHEDULE II	
FEES	
	<i>Rs. cts.</i>
1. Application Fees :	
(a) Manufacture of cigarettes	10,000.00
(b) Manufacture of cigars and beedi	100.00
(c) Import or Export of cigarettes, cigars, beedi, pipe tobacco, tobacco	7,500.00
2. Application Fees payable in respect of premises (Warehouses) :	
(a) Storage of raw materials for Manufacture of cigarettes	500.00
(b) Storage of cigarettes, finished products of pipe tobacco	500.00
3. Fees payable for the Transfer of Registration	10,000.00
4. Fees payable for the grant of a Certificate of Registration :	
(a) Manufacture of cigarettes	1,500,000.00
(b) Manufacture of cigars, beedi and pipe tobacco	500.00
(c) Storage of cigarettes, raw materials, finished products outside the manufacturing premises (These regulations shall apply to registered cigarette manufacturers and cigarette importers only)	50,000.00
(d) Storage of cigarette, raw materials within the premises separately	1,000.00
(e) Import tax (Each cigarette)	5.00

Source: Gazette No. 1625/1 - Monday, October 26, 2009.

While Schedule II of Gazette No. 1625/1 mandates the registration of manufacture and storage of cigars, beedi and piped tobacco (Figure 6), the manufacturing or sales of smokeless tobacco products are not subject to similar licensing or approval systems. Thus, overall compliance with Recommendation 3.1 is poor for OTPs.

Overall, the compliance with Recommendation 3.1 is evaluated as strong for cigarettes and poor for OTPs.

Recommendation 3.2: Adopt and implement measures and systems of storage and production warehouses to facilitate excise controls on tobacco products

Impact

Recommendation 3.2 is assessed as having a low impact score. The impact of this recommendation is indirect; it relates to storage and warehouse facilities that may make taxation easier, but does not discuss taxation itself. As is the case with most recommendations in this category, Recommendation 3.2 mainly addresses supply-related issues in order to facilitate better tobacco control.

Compliance

To facilitate better excise controls on tobacco, the FCTC recommends that authorities enforce suitable storage facilities and position persons at such locations to monitor production flows.¹²

For cigarettes, officers from the Departments of Excise and Customs are present at the manufacturing plants of CTC to monitor and facilitate taxation.¹³ Sri Lanka's compliance with Recommendation 3.2 is considered strong as there is only a single cigarette manufacturer with limited warehousing and tax collection points. However, as the compliance to this recommendation is not based on the tax authorities' ability to regulate, their capacity to independently facilitate the implementation of this recommendation represents a potential risk. In addition, the assessment of compliance for OTPs with Recommendation 3.2 is not relevant as most production is undertaken by informal cottage industries and does not entail storage and production warehouses as in the case of cigarettes.

Overall Recommendation 3.2 is evaluated with a strong compliance score on cigarettes and is considered not applicable for OTPs.

12. This individual would undertake tasks such as granting access to warehouses, handling pre-authorised visits, performing stock checks and controls, and coding and marking products.

13. Officers are rotated monthly.

Recommendation 3.3: Impose excise taxes at the point of manufacture, importation, or release from the storage or production warehouse for consumption

Impact

Recommendation 3.3 is assessed as having a medium impact score. The FCTC recommends implementing controls at the points of manufacture, import, and release for consumption. This reduces the complexity of administration and increases efficacy of tax collection. However, this recommendation also has no direct effect on tobacco consumption.

Compliance

For cigarettes, the Customs Officer at the CTC manufacturing plant is expected to observe the stock count and ensure that the stock is taxed before it leaves the premises. The ability of government agencies to implement similar controls on OTPs are limited due to the nature of the industries involved; they are largely informal and involve a large number of producers and importers. For example, the beedi industry has 700 licensed manufacturers. The Department of Excise does not have the resources to impose the necessary controls on these industries (as was the case with implementation of Recommendation 3.2). However, the few products (listed under Recommendation 1.2) are liable for excise and other tobacco taxes, which are taxed at a single point in the supply chain (such as beedi wrapper leaves at the point of import).

Overall, Recommendation 3.3 is evaluated as demonstrating a strong compliance score on cigarettes and a moderate compliance score for OTPs.

Recommendation 3.4: Require by law that tax payments are remitted at fixed intervals or on a fixed date each month

Impact

Recommendation 3.4 is assessed as having a medium impact score. Regularising tax payments sets a structure for information disclosure and tax collection, although it does not directly affect tobacco consumption.

Compliance

The Excise (Special Provisions) Act, No. 13 of 1989 mandates the quarterly payment of excise taxes (e.g. January to March quarter payments are due before 30th April the same year). Interviews with the Department of Customs revealed that excise taxes on cigarettes are collected at the end of each month (prior to the monthly rotation of the Customs Officials), showing that there are mechanisms in place for more frequent tax collection than mandated by legislation. In addition, taxes on tobacco inputs as specified by the Tobacco Tax Act, No. 8 of 1999 are collected by the Department of Excise every month. However, for OTPs not specified in the Act, there are no provisions in law for tax payments. At present, these products are also manufactured informally, making such an enactment difficult to implement.

Overall Recommendation 3.4 is evaluated with a strong compliance score on cigarettes and is considered not applicable for OTPs in Sri Lanka.

Recommendation 3.5: Report production and/or sales volumes, and price by brands, taxes due and paid, and volumes of raw material inputs

Impact

Recommendation 3.5 is assessed as having a medium impact score. Implementing this recommendation results in information disclosure, an important first step in ensuring due diligence and accountability when implementing tobacco tax and price policies. The availability of information on tobacco production and sales enables authorities to track current progress of tobacco control and design future regulations.

Compliance

The *Guidelines on WHO FCTC Article 6* suggests five information disclosure requirements: reportage of production and/or sales volumes, price by brands, taxes due, taxes paid, and volumes of raw material inputs. There has been some information disclosure with regard to cigarettes; the Handbook of Drug Information, an annual publication by the National Dangerous Drugs Control Board (NDDCB), contains three of the five information disclosure requirements (Table 6). The NDDCB publication does not, however, include information on taxes (current or past) due from cigarettes and unit prices though the latter can be obtained from other sources.¹⁴ Due to the relatively high level of information disclosure for cigarettes, the compliance score is evaluated as being high.

Table 6: Information disclosure of cigarettes

Description	Document	Data availability
Production	Handbook of Drug Abuse Information, NDDCB	Number of cigarette sticks, volume per brand; data available for previous year only
Tax paid	Handbook of Drug Abuse Information, NDDCB	LKR value per brand for the previous year only
	Annual Report, Central Bank of Sri Lanka	The total number of excise tax obtained from cigarettes
Input (volume)	Handbook of Drug Abuse Information, NDDCB	Number of tobacco kilograms used for the previous year only

Source: Handbook of Drug Abuse Information, NDDCB and Annual Report, Central Bank of Sri Lanka.

14. However, on cigarettes, unit taxes can be tracked by tracing government Extraordinary Gazettes published by the Department of Government Printing. Likewise, information on cigarette prices, though not formally published or reported by any institution, can be gleaned from various sources in the public domain, including retail outlets and media releases.

The publication or other official sources, however, do not contain similar information on OTPs. Proxy measures may be obtained if the OTP has raw materials that are imported, such as the case of beedi stick estimates discussed previously.¹⁵ Yet, there is no published information available on smokeless tobacco products. Consequently, compliance with Recommendation 3.5 for OTPs is poor.

Overall Recommendation 3.5 is evaluated at a strong compliance score for cigarettes and a poor compliance score for OTPs.

Recommendation 3.6: Tax authorities allow for the public disclosure of information

Impact

Recommendation 3.6 is assessed as having a medium impact score. Public disclosure of information (i.e., of data on tax and pricing) enables policy changes and allows public understanding of their impacts. In democratic societies, it is the latter and related discourse that acts as a substantial driver of government's responsibilities and diligence.

Compliance

Selected annual data on cigarettes are available in the Handbook of Drug and Information as discussed under Recommendation 3.5. However, although the Departments of Customs and Excise could publish monthly data on volumes and taxes collected from some tobacco products, they do not currently do so. As discussed previously, comparable information is not collected for OTPs, and information that is collected (such as the list of beedi manufacturers) is not publicly disclosed.

As such, the proactive disclosure of information by the relevant agencies is weak, and obtaining information through them is difficult. In this regard, Sri Lanka recently passed the Right to Information (RTI) Act, No 12 of 2016, that allows individuals to request information available within government organisations and bridge the data deficit highlighted under this recommendation. While the implementation of the Act is still ongoing, this is nevertheless a development in the positive direction.

Overall, Recommendation 3.6 is evaluated to a moderate compliance score for both cigarettes and OTPs.

15. For example, beedi consumption is calculated by obtaining import data on the tendu leaf from the Department of Customs and estimating its contribution to a single stick of beedi often using the conversion rate of 2000 beedi sticks from one kilogram of tendu leaf (Common conversation rate of 2000 is adopted from: Arunatilake & Opatha (2003), and conversations with beedi manufacturers who claimed 1kg of beedi could produce 2000 beedi sticks of 2.5 inches). This rate can be contested as all sources have relied on beedi manufacturers who are likely to produce varying lengths of beedi that may not be captured in the calculation. Lal (2011) has noted one tendu leaf is able to make one beedi and with 50,000 leaves weighing 40kgs, the conversion rate is 1,250 beedi for every kilogram.

Recommendation 3.7: Impose effective anti-forestalling measures, in anticipation of tax increases

Impact

Recommendation 3.7 is assessed as having a medium impact score. The FCTC defines forestalling as the increase in production/stock of a product in anticipation of a tax increase. When taxes are implemented at predictable times of the year (such as the second reading of the national government budget done annually in November), producers are able to anticipate a tax increase and thereby take advantage of an existing lower tax rate by drastically increasing production. This reduces the potential revenue earned from the tax increase by the government. To prevent forestalling, the FCTC recommends restricting excessive production before tax increases and imposing the taxes on existing stock prior to distribution. This recommendation enables taxation measures to be reflected more effectively in pricing and discouraging market manipulation and black-market activities.

Compliance

The current legislation does not provide any specific measures to prevent forestalling. While government authorities do collect monthly data regarding cigarette production that allows for an assessment of the degree of forestalling, they do not raise concerns of forestalling.¹⁶ As such, there are no legislative provisions or measures against forestalling in place. This issue is also present for OTPs, though the proliferation of the informal sector in this case would make such measures more difficult to implement.

Overall Recommendation 3.7 is evaluated at a score of non-compliance for both cigarettes and OTPs.

Recommendation 3.8: Require application of fiscal markings

Impact

Recommendation 3.8 is assessed as having a medium impact score. Fiscal markings are tax stamps, enhanced tax stamps (banderols) or digital tax stamps that ensure that a producer complies with tax laws.¹⁷ Fiscal markings also enable authorities to distinguish between legal and illegal tobacco products and are useful in tracking the distributor system of illicit trade (WHO FCTC, Article 15). While it is a mechanism of working against illicit supply, it does not directly impact demand.

16. To assess the degree of forestalling, at least weekly and monthly data on tobacco production, sales and stocks are needed. This allows for an analysis of abnormal (forestalling) activity both before and after-tax increases are imposed.

17. Enhanced tax stamps (banderols) require monitoring scanners at production facilities read the tax stamp and electronically transfer the information to Ministry of Finance. The live transmission would contain information such as the number of packs produced and relevant production factory. Digital tax stamps are similar to enhanced tax stamps and provide effective tracking and tracing systems. The primary difference is its method of operation. Digital stamps require distributors to first request for an order of cigarettes from a designated authority. Upon verification of the request, the distributor then delivers the products. World Health Organisation (2010). WHO Technical Manual on Tobacco Tax Administration.

Compliance

Currently, fiscal markings are not imposed on cigarettes (sticks or packets) or on any OTPs. There are no distinguishable characteristics on tobacco products that may aim to fulfil the objectives of the fiscal marking, making them non-compliant with the recommendation.

Overall Recommendation 3.8 is evaluated with a score of non-compliance for both cigarettes and OTPs.

Recommendation 3.9: Clearly designate and grant appropriate powers to tax enforcement authorities

Impact

Recommendation 3.9 is assessed as having a medium impact score. The effectiveness of this recommendation is largely on curbing inefficiencies in tax administration. Effective tax administration and enforcement requires a clear definition of each authority's capacity to investigate, search, seize, retain and dispose of tobacco products. Clarifying each authority's jurisdiction facilitates effective tax measures and ensures the level of control needed to properly implement those measures.

Compliance

Sri Lanka's tobacco control legislation states the names, powers and responsibilities of the relevant authorities. The NATA Act recognises Food and Drug Inspectors, Public Health Inspectors, Police Officers, and Excise Officers as Authorised Officers under the Act (Articles 16 & 17). In the event an Authorized Officer has reasonable grounds to believe there has been a violation of the act, their mandated powers include:

- (a) at any reasonable time enter any place where he believes any tobacco product or alcohol product is manufactured, prepared, preserved, packaged, exposed for sale or stored and examine any such tobacco product or alcohol product and take samples thereof and also examine anything that he believes is used for the manufacture, preparation, preservation, packaging or storing of that tobacco product or alcohol product;
- (b) for the purpose of carrying out effective search operation, stop or detain any vehicle in which he believes that any tobacco product or alcohol product is being conveyed, search that vehicle and examine any tobacco product or alcohol product which is being so conveyed and take samples thereof;
- (c) open and examine any receptacle or package that he believes contains any tobacco product or alcohol product;
- (d) seize and detain for such time as may be necessary any tobacco product or alcohol product by means of, or in relation to which he believes any provision of this Act or regulation made thereunder has been Contravened'

Source: Article 17 of National Authority on Tobacco and Alcohol Act, No. 27 of 2006.

Although the NATA Act governs all tobacco products under its purview, the lack of information and regulations specific for OTPs has resulted in the prioritization of cigarettes over OTPs. That is, while adequate powers are delegated, their practical operationalisation is much higher for cigarettes than for OTPs. Therefore, compliance with Recommendation 3.9 is strong for cigarettes but poor for OTPs.

Overall, Recommendation 3.9 is evaluated to a strong compliance score on cigarettes and a poor compliance score for OTPs.

Recommendation 3.10: Provide for information sharing among enforcement agencies in accordance with national law

Impact

Recommendation 3.10 is assessed as having a medium impact score. The implementation of this recommendation will improve the access and use of information between government departments and bodies that have an interest in tobacco control or have their areas of interest affected by tobacco control policies. Sharing learning and experiences between enforcement agencies will both inform decision making and help drive sustainable policies.

Compliance

The NATA Act includes provisions for information sharing between government agencies for the administration and enforcement of the Act (Article 17 (3)). Subsection 4, Article 17 of the Act states that “information obtained by an Authorized Officer under subsection (3) shall not be disclosed except to a Government Department or to a Court unless other [wise it] is required for the purposes of administration or enforcement of this Act”.

Overall, Recommendation 3.10 is evaluated to a strong compliance score for both cigarettes and OTPs.

Recommendation 3.11: Provide for an appropriate range of penalties to deter non-compliance with tax laws

Impact

Recommendation 3.11 is assessed as having a medium impact score. Penalties act as deterrence to the non-compliance of tax laws. The FCTC indicates that if parties forgo their tax-related obligations, penalties including (but not limited to) cancellation of licence, fines, imprisonment and forfeiture of assets must be imposed. However, penalties alone cannot facilitate effective taxation; the relevant authorities need to possess the technical capacity to administer the penalties.

Compliance

Article 16 of the Excise (Special Provisions) Act, No. 13 of 1989 states that parties involved in the production and distribution of selected tobacco products that fail to comply with the excise tax measures (such as by defaulting on tax payments and failing to furnish tax returns) will have their registration/license suspended and may be subject to judicial prosecution (Article 26). However,

as discussed before, these provisions are limited to the effective tax administration of cigarettes.¹⁸

Additionally, current tax non-compliance penalties imposed on cigarettes and OTPs are unlikely to have a strong deterrent effect. This is partly due to the value of penalties being unchanged over time. It must be noted that it is also difficult to assess the impact of a penalty in place over time, because data regarding offences committed under the relevant Acts is not available.

Overall Recommendation 3.11 is evaluated to a medium compliance score for both cigarettes and OTPs.

3.5. Category 4: Use of revenues - financing of tobacco control

The *Guidelines for Implementation of Article 6* highlights the importance of taxation and pricing for contributing to government revenue. The FCTC recognises that tobacco taxation could be used to enhance tobacco controls by providing allocations for tobacco control programmes (Table 7).

Table 7: Evaluation for recommendations under Category 4

Recommendation	Impact	Compliance	
		Cigarettes	OTPs
4. Use of revenues – financing of tobacco control			
4.1 Dedicate revenue to tobacco control programmes	Low (1)	Poor (1)	Poor (1)

Recommendation 4.1: Dedicate revenue to tobacco control programmes

Impact

Recommendation 4.1 is assessed as having a low impact score. The FCTC allows parties the sovereign right to establish taxation policies and expenditure allocations for relevant taxes. The *Guidelines for Implementation of Article 6* recommends taxes charged on tobacco products be used for tobacco control programmes such as health promotion and disease prevention, awareness raising and cessation services. While a dedicated revenue stream for tobacco control will gradually reduce tobacco consumption, this alone does not guarantee adequate funding for relevant programmes to reduce tobacco consumption.

Compliance

18. There is evidence of enforcement agencies imposing penalties for offences. For instance, the Annual Report of the Department of Excise lists several offences committed and relevant fines collected under the Tobacco Tax Act and NATA Act. However, the admissions and offences for tobacco products is not specified.

At present, anti-tobacco programmes, such as awareness programmes and cessation services, are implemented by NATA and the Ministry of Health, Nutrition and Indigenous Medicine. While these agencies receive a central government budgetary allocation for their recurrent and capital expenditure pertaining to administration activities, they do not receive any dedicated government funding for tobacco control activities. Funding that NATA does secure for tobacco control for instance, is generally from international organisations and for short to medium-term projects. As such, this type of funding does not guarantee a steady funding source for tobacco control programmes.

Overall, Recommendation 4.1 is evaluated as demonstrating a poor compliance score for both cigarettes and OTPs.

3.6. Category 5: Tax-free/duty-free sales

While taxation is a primary form of tobacco control, the FCTC recognises that restricting duty-free market places is also important for curbing tax avoidance (WHO, 2010), which in turn will reduce tobacco consumption (Table 8).

Table 8: Evaluation of recommendations under Category 5

Recommendation	Impact	Compliance	
		Cigarettes	OTPs
5. Tax-free/ Duty-free sales			
5.1 Prohibit or restrict the sale to and importation by international travellers, of tax-free/ duty-free tobacco products	High (3.5)	Strong (8)	Strong (8)

Recommendation 5.1: Prohibit or restrict the sale to and importation by international travellers, of tax-free/ duty-free tobacco products

Impact

Recommendation 5.1 is assessed as having a high impact score. Ports of entry, such as airports, often offer tax-free tobacco products. As taxes are a primary form of discouraging consumption, the availability of duty-free tobacco products reduces the impact of taxes (and subsequent higher prices) on consumers entering or leaving a country. Thus, selling duty-free tobacco products is counterproductive to both the social incentive of reducing tobacco consumption and the economic interest of increasing tax revenue. The FCTC recommends prohibiting duty-free tobacco products, imposing excise taxes on all tobacco products and stores, and imposing a quota for travellers for the purchase of duty-free tobacco products. The impact of this recommendation on tobacco consumption is that it prevents demand from shifting and growing through alternative tax-free channels.

Compliance

Duty-free shops that operate in the Sri Lankan airport are restricted in their sale of tobacco products. They are prohibited from selling tobacco products to arriving passengers, discouraging relatively cheaper tobacco products to be brought into the country. However, the duty-free outlets preceding the departure terminals at the Bandaranaike International Airport do openly display cigarettes, allowing for those leaving the country to purchase cigarettes. However, as this criterion only considers controls on domestic consumption, Sri Lanka's compliance with Recommendation 5.1 is evaluated as strong for all tobacco products.

Overall recommendation 5.1 is evaluated as demonstrating a strong compliance score on both cigarettes and OTPs.

4

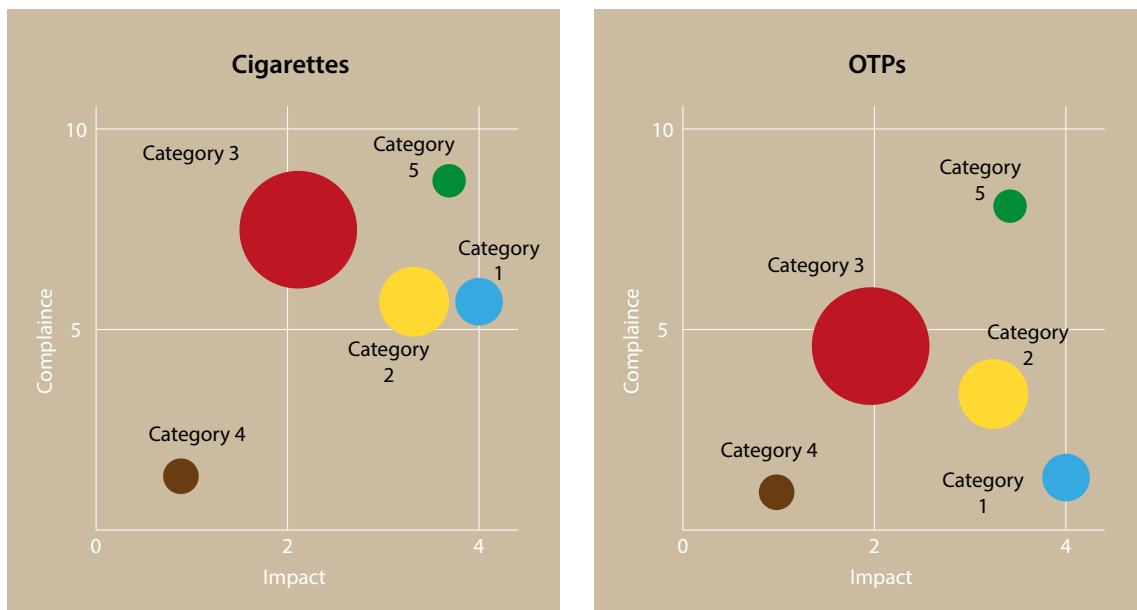
Analysis of the FCTC Article 6 impact and compliance

Section 3 estimated scores on impact and compliance for each of the 19 recommendations identified under Article 6 of FCTC. This section makes further inferences on four levels of analysis: category-level analysis, product gap analysis (between the cigarettes and OTPs), recommendation-level analysis and compliance-level analysis.

4.1. Category-level analysis

The category level maps out the difference in compliance and impact between the five categories. It also provides an analysis of the response implication for each category. The scores assigned to each of the recommendations can be aggregated by categories to reflect the average estimation of impact and compliance by category. These categories based on average scores are set out in Figure 7, along two axes. The impact score is measured on the horizontal axis and the compliance score is measured on the vertical axis. Figure 7 sets out the results separately for cigarettes and for OTPs. The size of the marker indicates the number of recommendations under each category.

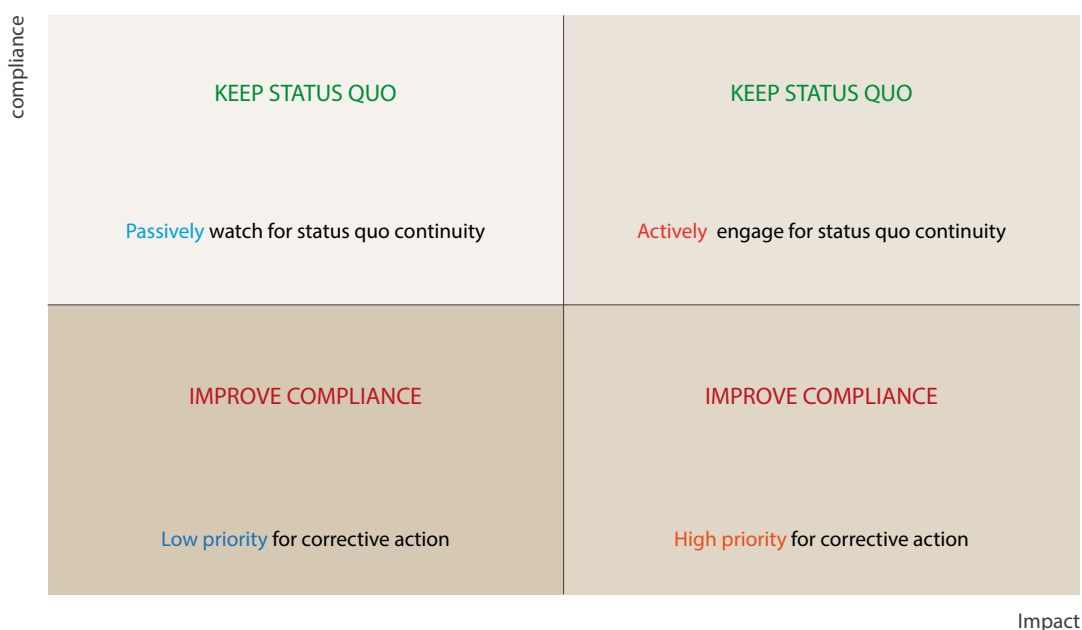
Figure 7: Average scores of impact and compliance of FCTC recommendation categories



Source: Based on Author's assessment in Section 3.

The quadrants in figure 8 should be interpreted as follows. If compliance and impact places any category in the bottom right quadrant (high impact, low compliance), then it is of higher priority for action and rectification. Those that are in the top left-hand quadrant (low impact, high compliance) will be those that are low priorities for rectification/action.

Figure 8: Average scores of impact and compliance of FCTC recommendation categories



Using the above guidance framework for prioritisation, we can take a closer look at the response that is relevant to each category.

The focus of the recommendation under each category can be summarised as follows:

1. Link taxes to prices and public health
2. Effective tax system and monitoring
3. Improve tax administration
4. Dedicate tax revenue for control
5. Prevent duty free sales

Category 1 recommendations are about the relationship between tobacco taxes, price and public health. There are two recommendations in this category. The first is concerned with the process and evaluation of adjustments in taxes and prices and the second with the method and calculation of those adjustments. The recommendations in this category have the highest level of average impact (4/4). However, the compliance level at 5.5 is the second lowest (for cigarettes this is true of Category 2 as well) and at 1.5 is the second lowest for OTPs as well.

This means that **Category 1** recommendations are a **high priority for corrective action**, and they require **active engagement to continue with existing compliance measures and improve compliance**.

Category 2 relates to the effectiveness of the tax system and monitoring. It has four recommendations relating to the types of taxes imposed, the consistency of tax treatment across tobacco products, regular monitoring, and a long-term tobacco policy. The average impact of the recommendations in this category are high (3.4/4) and yet the compliance levels are the second lowest for cigarettes (at 5.5) and low for OTPs (at 3.3).

This means that **Category 2** recommendations are also a **high priority for corrective action**, and they require **active engagement to continue with existing compliance measures and improve compliance**.

Category 3 relates to improving tax administration. It has eleven recommendations addressing the licencing of production, excise tax controls (point of taxation and its payment, warehouses, fiscal markings, anti-forestalling measures), information disclosure (production, tax, price and raw material) and tax enforcement (clarity in enforcement authorities and penalties). The average impact of the recommendations in this category are at a medium level (2/4), and have the second highest compliance level of all categories: 7.1 for cigarettes and 4.1 for OTPs.

This means that **Category 3** recommendations are a **medium priority for corrective action**, and they could also require **passive and active engagement to continue with existing compliance measures**.

Category 4 relates to dedicating tax revenue for tobacco control. It has only one recommendation in this regard. That recommendation has the lowest level of average impact (1/4). It also has the lowest level of compliance for all tobacco products (at 1/10).

This means that the **Category 4** recommendation is a **low priority for corrective action**, even while

it still requires **attention to improve compliance**.

Category 5 relates to preventing duty free purchases and sales. It has only one recommendation in this regard. That recommendation has the highest level of average impact (3.5/4). It also has the highest level of compliance (8/10), for both cigarettes and OTPs.

This means that **Category 5** recommendations require **little corrective action**, but require **active engagement to continue with existing compliance measures**.

Overall, it is the recommendations of Categories 1 and 2 (linking taxes to prices and ensuring an effective system and monitoring) that are most important in terms of focusing corrective action.

4.2. Inter- and intra-product gap analysis

There are two kinds of gaps in compliance that are teased out in this section. One is the compliance gap in categories between product types (this is called the inter-product gap). The second is the compliance gap in categories within product types (this is called the intra-product gap).

Inter-product gap: Overall, OTPs fare relatively poorly with regard to compliance on the FCTC, both in absolute terms and also in comparison to cigarettes. The gap in compliance scores between the two product types are notable: the inter product gap in compliance between cigarettes and OTPs is highest for Category 1 (cigarette and OTP difference is 4.0). There is no significant difference in compliance evaluated between these product types for Categories 4 and 5. It is second and third highest for Categories 3 and 2, respectively. There is a gap of 3 for Category 3 and a gap of 2.2 for Category 2.

Intra-product gap: There is also an intra-product gap in compliance. The greatest gap for both cigarettes and OTPs is between Categories 4 and 5 (a gap of 7, with compliance scores of 1 and 8). For cigarettes, compliance scores are the same for Categories 1 and 2 (both at 5.5) while for OTPs there is a gap in compliance for these two categories (1.5 for Category 1 and 3.3 for Category 2). For both product types Category 3 pulls ahead of Category 1 and 2, at 7.3 for cigarettes and 4.3 for OTPs.

4.3. Recommendation-level analysis

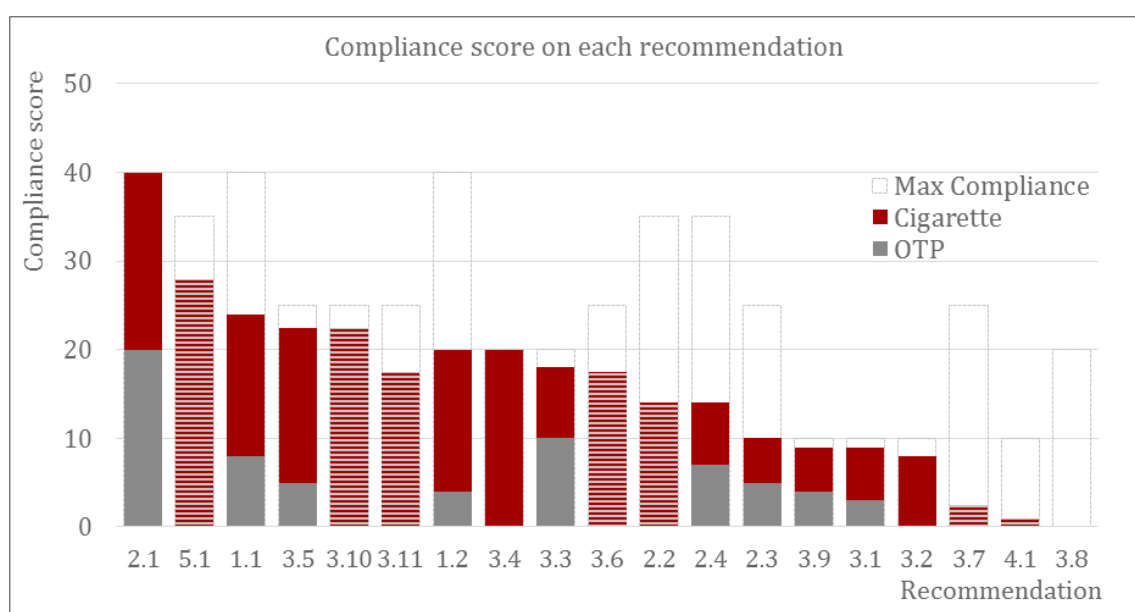
This section looks at each of the recommendations and compares compliance on cigarettes and OTPs against the impact weighted potential for full compliance.

The compliance scores assigned to each of the recommendations can be reported as a weighted score to capture the impact significance of compliance. What this means is that compliance on a recommendation with high impact is more significant than compliance on a recommendation with a impact. Figure 9 sets out the weighted compliance scores for each recommendation.

Figure 9 looks at the nineteen individual recommendations of the two tobacco products sorted according to their weighted compliance score. The dotted outline of the columns marks the maximum score that can be obtained for a recommendation (maximum score based on impact). The weighted compliance scores are marked on the Y axis with the cigarette compliance scores shown in red and OTP compliance scores in grey.

Note that in the graph, the two products' scores are overlapped. Therefore, when the red shows above the grey, it means that the compliance score for cigarettes is higher, and if the grey showed above the red, the compliance score for OTPs is higher. Columns with red and grey stripes indicate the recommendations where cigarettes and OTPs record the same weighted compliance score. The result shows that all scores for cigarette compliance are equal to or higher than OTPs. Five recommendations have equal scores, including Recommendation 3.8 (anti-forestalling measures) where it was not possible to find any evidence of compliance. For cigarettes, the two Recommendations 2.1 and 3.4 have achieved the maximum possible compliance score.

Figure 9: Impact weighted score of compliance of FCTC Article 6 recommendations



Note: Tobacco product scores for Recommendation 3.2 and Recommendation 3.4 is not 0, but the compliance is N/A.

Source: Based on Author's assessment in Section 2.

4.4. Compliance level analysis

When the recommendations are subdivided in terms of compliance, the following patterns and details emerge:

- The recommendations with high compliance deal with restricting the sale of duty-free tobacco products, clarifying the jurisdiction of regulatory authorities, imposing penalties on tax related violations, and implementing cigarette excise taxes.
- The recommendations with moderate compliance deal with regular adjustments of cigarette tax and controls on licensing.
- The recommendations with weak compliance relate to implementing methodical tax increments and creating a long-term policy on taxation. Reforming policy on tobacco tax is important because tax and price of tobacco products have a high impact on limiting tobacco demand.
- There are recommendations with zero compliance as well, such as the application of fiscal markings (on available information).

5

Recommendations

The FCTC's recommendations include a national strategy that sets out targets (such as tax and price level targets), awareness and health programmes, which would allow policymakers to track progress on specific goals and celebrate milestones of achievement. Regarding obstacles to implementation, this evaluation identifies three.

- 1.** The first is the most important. It is the lack of an explicit and performance targetted long-term national strategy to reduce tobacco consumption through both tax/price and non-price measures.
- 2.** The lack of a structured taxation system on tobacco products, which often prevents the timely adjustment of taxes and has resulted in cigarettes being more affordable today than they were two decades ago.
- 3.** Third is the limited availability of information on tobacco taxes and production which makes it difficult to monitor, assess and report on tobacco control.

The second and third issues are secondary to the first, as creating a structured tobacco control strategy would address these concerns.

Table 9 outlines measures that would enable greater compliance with the FCTC requirements in the context of a long-term national policy on tobacco control.

Table 9: Measures to improve FCTC compliance

Measure	Responsibility	Time-frame	Output/ Performance Indicator	Outcome
1. Sound tobacco taxation system				
1.1 Develop specific tax formula for cigarettes	NATA/ Ministry of Finance (MoF)	Short term	A publicly known tax formula that takes into account real income growth and is developed on a technically rigorous basis	Affordability of cigarettes does not fluctuate unevenly over time
1.2 Study the operational and regulatory environment of OTPs	NATA	Short term	Supply chain mapping, surveys and data collection for OTPs	Availability of regular data on price, volume, tax revenue etc., and therefore the ability for better decision-making about efficient taxation of OTPs
1.3 Adjust tax levels at regular intervals for both cigarettes and OTPs	MoF	Medium term	A system that periodically increases taxes and also addresses forestalling	Affordability of tobacco products do not fluctuate unevenly over time
1.4 Revisit tax formula every five years for both cigarettes and OTPs	NATA	Long term	Review historical tax performance	Affordability of tobacco products does not fluctuate unevenly over time
1.5 Monitor taxes and prices within and between tobacco products and take corrective action where relevant	NATA/MoF	Continuous	Regular collection of data and application of the price formula and affordability measures across the board	Price increases on all tobacco products are structured to take account of consumer response and to minimise substitution
2. Reduce information asymmetry				
2.1 Proactively disclose the monthly prices of cigarette brands (both historical and current)	CTC/MoF	Continuous	The information becomes accessible without the need to file tedious Right to Information Requests.	Improved information available for formulating sound tobacco control policies
2.2 Introduce vendor licensing for cigarettes and beedi	Excise Department	Short term	Vendor list	Improved information regarding the sales of cigarettes and beedi
2.3 Disclose information on imports of raw material for beedi production	Department of Excise/ Department of Customs	Medium term	Data available in the Handbook of Drug Information	Availability of data for the application of a tax formula

Measure	Responsibility	Time-frame	Output/ Performance Indicator	Outcome
2.4 Publish information on sales volume and price for each cigarette brand and on taxes (due and paid) for OTPs	NDDCB/ Department of Customs	Medium term	Data available in the Handbook of Drug Information	Availability of data for the application of a tax formula

Over a decade has passed since Sri Lanka ratified the WHO FCTC. Sri Lanka's efforts in the early stages following the FCTC were marked by significant activity through the establishment of laws and authorities for tobacco control. During this time, Sri Lanka's implementation of the FCTC recommendations had community support and political-backing.

However, an evaluation of the recommendations under Article 6 of the FCTC indicate that Sri Lanka's tobacco taxation and price policies can be improved significantly. The evaluation also notes that there is stronger control on cigarettes than OTPs. The achievements in compliance on cigarettes with regard to a number of recommendations can be attributed in part to the fact that cigarette production and supply in Sri Lanka is a monopoly industry and comes under adequate oversight of regulatory authorities. In contrast, OTPs operate in an informal industry.

Although cigarettes are the primary vehicle of tobacco consumption in Sri Lanka, the other smoked and non-smoked tobacco products in use should not be overlooked by tobacco control laws. In this regard, the evaluation recognises the importance of accurate and timely information for sound tobacco control and tax administration.

In addition, the overall compliance of the FCTC recommendations require much improvement both within the tobacco product categories and among tobacco products.

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