



30 January 2014

Mr Jason McNamara
Executive Director
Office of Best Practice Regulation
Department of the Prime Minister and Cabinet
John Gorton Building
King Edward Terrace
PARKES ACT 2600

Email: helpdesk@obpr.gov.au

Dear Mr McNamara *Jason*

DETAILS-STAGE REGULATION IMPACT STATEMENT - INCREASING EXCISE AND EXCISE-EQUIVALENT CUSTOMS DUTY ON TOBACCO AND TOBACCO PRODUCTS

I am writing in relation to the attached details-stage Regulation Impact Statement (RIS) prepared by the Treasury for increasing excise and excise-equivalent customs duty on tobacco and tobacco products.

I am satisfied that the details-stage RIS meets the Government's best practice regulation requirements with the problem being adequately explained, the objectives of government action well-articulated; and impacts on various stakeholders well-explained.

We have sought to meet OBPR requirements as outlined in your letter of 15 November 2013 and subsequent emails of 14 January 2014 and 22 January 2014.

In the letter of 15 November 2013 OPBR requested the following additional material be added to the RIS:

- the need for a quantification of business costs using OBPR's business cost calculator (BCC) as agreed to by OBPR;
- consultation with a range of appropriate stakeholders;
- check list and conclusion statement on compliance with the options RIS;
- more in depth analysis in the problem and the impact section;
- the Option needs to explain the proposal is an election commitment so alternative options are not required to be considered;
- The conclusion section should be reviewed to ensure it gives a balanced account of the preceding analysis.

In response to this letter Treasury undertook the following:

- prepared a BCC costing in consultation with OBPR and the deregulation area in Treasury;

- carried out a consultation with industry (3 major tobacco companies who are manufacturers and wholesalers) and with retailers (including through their industry associations) – this consultation was also carried out in response to OBPR’s email of 14 January 2014);
 - this consultation was carried out by correspondence and apart from the short timeframe consultees appeared satisfied with the consultation process;
 - other stakeholders such as health and consumer representatives were not consulted as part of the RIS as they have been consulted as part of the broader strategies to reduce smoking in Australia;
 - the consultation process allowed stakeholders to confirm Treasury’s analysis of the estimated impacts of the tobacco excise measures or provided the opportunity to stakeholders to provide an alternative view;
- inserted a check list and conclusion statement on compliance with the options RIS;
- dealt with further issues raised on the Problem and Impacts. Further information on how each of the points raised in OBPR’s letter of 15 November 2015 and later emails is addressed at Attachment A.
- modified the conclusion section so that it gives a balanced view of the preceding analysis.

I submit the certified RIS to the Office of Best Practice Regulation for formal assessment.

Yours sincerely



Rob Heferen
Executive Director
Revenue Group
Treasury

OBPR comment	Treasury response
Problem	
<p>In relation to the identified information failure:</p> <ul style="list-style-type: none"> • To what extent/among which age demographics are smokers not fully informed of the risks of becoming addicted to smoking? • To what extent are smokers not aware of the long-term health effects of prolonged smoking? • Given the number of information campaigns on the health effects of smoking undertaken by private and public actors, how does the information failure arise? 	<p>Treasury inserted a new section dealing with information failure and addresses these three issues to the extent that research has been carried out and the information is available. The Department of Health provided numerous references from studies and research and these have been referenced in the RIS.</p> <p>This section is also linked to smoker behaviour. In the Benefits section the RIS address the loss of benefit for individuals and society from anti-smoking measures because of smoker behaviour.</p>
<p>In relation to the externalities:</p> <ul style="list-style-type: none"> • What factors are understood to drive the social health and economic costs of smoking? • What are these costs and against which counterfactual are they being assessed? • What is the direct cost of treating smoking-related illness for an individual, compared with (for example) other costs associated with those non-smokers who may live considerably longer (aged care, social security payments, etc)? In other words, are the direct costs of smoking-related illnesses substituting for other health costs, and are they therefore truly avoidable? <p>In an email of 22 January 2014, OBPR advised the RIS should include an assessment of the avoided government expenditure resulting from the lower government expectancy of smokers versus non-smokers. In other words, the RIS will need to assess what are the counterfactual long-term health costs associated with longer survivorship of non-smokers. OBPR provided a link to the Collins and Lapsley report.</p>	<p>After further information was obtained from the Department of Health, the social and economic impacts of smoking are now comprehensively discussed in the RIS.</p> <p>This is mainly achieved by referring to a study by Collins and Lapsley (2008), which is the latest and most definitive research that the Department of Health uses as the estimate of the social and economic costs of tobacco use.</p> <p>This study also considers the counterfactual long term health costs associated with longer survivorship of smokers and the RIS contains a discussion of the counterfactual scenario used by Collins and Lapsley.</p> <p>The RIS also references other studies which note that the Collins and Lapsley study took a conservative approach to the estimation of costs.</p>
<p>In relation to the regulatory failure:</p>	<p>Treasury has inserted into the RIS a comprehensive overview of the current regulatory framework,</p>

<p>The RIS should include a more detailed discussion of the current regulatory/policy framework, and why further Government intervention is justified.</p> <p>The RIS currently canvasses existing government policies aimed at decreasing the affordability of cigarettes. The RIS should also outline other related policies aimed at discouraging tobacco use, such as restrictions on advertising, public information campaigns and restrictions on smoking in public places.</p> <p>Consequently, the RIS should provide an assessment of the efficiency and effectiveness of current regulations. This could include:</p> <ul style="list-style-type: none"> • Quantification of how successful these policies have been in reducing smoking; and • Quantification of the cost of implementing these policies (compliance and administrative) relative to reductions in smoking. For example, what is the dollar cost of each percentage reduction in smoking achieved from the respective policies? 	<p>describing anti-smoking measures and stressing the importance of a multi-pronged approach in reducing smoking levels.</p> <p>The RIS contains diagrams which show the decline in smoking rates and includes a diagram which links the decline with policy interventions.</p> <p>The RIS explains the importance of price and tax measures and how they act synergistically with other measures to bring down smoking.</p> <p>The RIS explains that it is not possible to quantify in dollar terms the benefits from separate measures but refers to a study that has sought to quantify the benefits in total.</p> <p>Compliance and administrative costs (ACBPS, ATO and industry) are discussed in the impacts section.</p>
<p>Additional issues</p> <p>The RIS should include a more detailed assessment of the income and other effects of the policy on individuals and households.</p> <p>For example, the discussion on page 2 notes that lower income households are particularly vulnerable to the opportunity cost of expenditure on tobacco products. The RIS should provide greater depth to the discussion of income and other relevant demographics among smokers (age, cultural, or Indigenous, etc) and the implications of this from an individual and households income perspective.</p> <p>In terms of the private impacts of smoking, the RIS provides an overview of the general costs and benefits. It would be useful for the RIS to explain if it is considered that, on balance, smoking imposes a net cost or benefit for individuals. That is, is it considered that the private benefits of smoking outweigh its private costs?</p> <p>If it is considered that there is a net cost from smoking the RIS should explain what (if anything) is impeding smokers from making an informed</p>	<p>The RIS now contains a discussion (based on the information that is available) on the income and other effects of the policy on individuals and households. It examines:</p> <ul style="list-style-type: none"> • elasticities among various groups (including the young versus adult and low income versus high income); • impact on different socio-economic groups including latest data on Indigenous smoking rates and rates for pregnant mothers, the mentally ill and those who are unemployed; • the implications for lower income groups in terms of cost and research and expert opinion as to whether this group will be more disadvantaged by the measures. <p>The RIS does not address private benefits of smoking as the Department of Health considers this was not relevant in a public policy context and there is no suitable research indicating that there are any benefits to smoking. Minor health benefits that were identified in the Collins and Lapsley report have been included.</p>

<p>assessment of the expected costs and benefits of smoking.</p> <p>In an email of 14 January 2013 OBPR also requested more development of the externality argument in information and the counterfactual long-term health costs associated with longer survivorship of non-smokers.</p> <p>It also stated that the problem section would benefit from greater balance. For example, the RIS could explicitly acknowledge that the correlation between implementation of policies and decline in smoking rates may be temporally but not causally related. Smoking rates may have declined in the absence of policy intervention (albeit at a slower rate).</p>	<p>The RIS deals with smoker behaviour and information failure which impedes smokers from making an informed assessment of the expected costs and benefits of smoking.</p> <p>Treasury considers that the RIS addresses the link between policy interventions and the decline in smoking rates.</p>
<p>Impacts</p>	
<p>As noted above, the RIS should provide a more detailed discussion of the potential impacts of the excise increase on different groups in society, such as low-income households and indigenous households. For example, the RIS could consider the distribution effects of the proposal on low-income and indigenous groups. To achieve this the RIS could consider the following:</p> <p>What is the price elasticity of demand among low-income and indigenous demographics relative to other demographics?</p> <p>What are the potential implications for those in these demographics who do and do not quit smoking following the excise increase?</p>	<p>See Problem above.</p> <p>Treasury and the Department of Health have researched studies dealing with price elasticities and have included their findings in the RIS.</p> <p>As outlined above, the RIS considers the implications for more disadvantaged socio-economic groups. This includes a table which indicates additional tax discusses and prices rises that may result from the excise increase.</p> <p>It also points out that an investment in other tobacco measures such as subsidised smoking cessation aids, will improve the situation of low income people,</p>
<p>The impacts analysis should include more depth in relation to impacts on cigarette producers, both in an economic sense and in relation to compliance. For example:</p> <p>What precisely is required in terms of excise collection and changes to systems/pricing?</p> <p>What are the current sales volumes/profits of the large cigarette manufacturers – how significant is the industry?</p> <p>What have been the trends in production/sales over</p>	<p>Treasury has consulted with the ATO, ACBPS and industry stakeholders to determine the impact of the excise increases.</p> <p>The results of consultation and the findings of a Post-implementation Review carried out after a 25 per cent increase in excise as from 29 April 2010 are also included in the analysis.</p> <p>The RIS now contains industry data from a recently commissioned KPMG report and from IBISWorld.</p>

<p>the past years – and to what extent are changes in revenues likely to be attributed to increases in the rate of excise?</p> <p>Is there any minimum efficient scale below which it will not be feasible to manufacture/wholesale/retail cigarettes, and are there any indications that further planned increases in the excise rate may prompt withdrawal from the industry by one or more supply chain participants?</p>	<p>We were not able to find any data of any minimum efficient scale below which it will not be feasible to manufacture/wholesale/ retail etc. There are some comments of a more general nature from stakeholders that address this issue, noting that tobacco production is a declining industry in Australia.</p>
<p>The impacts analysis should also canvass the impacts on distribution businesses, including specialty tobacco importers and retailers:</p> <ul style="list-style-type: none"> • Are there any distributional issues, for example disproportionate impact on small businesses? • What action will retailers need to take to comply, eg. updating their prices and displays etc? 	<p>Treasury has consulted with the 3 major tobacco companies and retailers. These stakeholders retailers have indicated the impact of these measures and their comments are included in the RIS.</p> <p>Consultation was not undertaken with duty free stores, providores and importers as this group is identified as being small in IBISworld. The ATO and the ACBPS supported the view that there would be minimal benefit from tracking down these businesses where impacts are likely to be minimal.</p> <p>These groups were not consulted as part of the Post-implementation review for the 25 per cent excise increase.</p>
<p>The RIS currently posits that staged tobacco increases are not likely to create any significant distortion in business decision-making by the tobacco companies. It is difficult to understand how this can be possible if the policy is to result in a significant reduction in smoking. If the claimed lack of distortion is related to the relative inelasticity of demand, then this argument should be discussed in a manner consistent with the claimed health benefits that flow from the proposal. The RIS should also explain if this view is supported by stakeholder consultation.</p>	<p>Treasury supports OBPR's assessment that the staged increases could change business decision making. This is discussed in the RIS. As well the RIS discusses how the measure will impact on consumer decision making.</p>