

EVALUATION OF STATE LEVIES POLICY ON CIGARETTE AND E-CIGARETTE

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ABSTRACT:

Cigarettes and e-cigarettes are goods that have negative externalities. Due to the negative externalities, the government needs to control the consumption of these two goods with the imposition of state levies. From this background, this study discusses the evaluation of policies on state levies imposed on cigarettes and e-cigarettes. This study aims to determine the structure of state levies imposed on cigarettes and e-cigarettes, and to know the differences in treatment of state levies on cigarettes and e-cigarettes. This research has qualitative research with descriptive research types. The results of this study found that conventional cigarettes consisted of three levies, that was Excise, VAT Tobacco Products, and Cigarette Tax, while e-cigarettes consisted of two levies, namely Excise and VAT Tobacco Products. In addition, it was also found that the difference in treatment of state levies on conventional cigarettes and e-cigarettes, the first there was a difference in excise rates for the two goods, and the second there were differences in the treatment of cigarette tax imposition on the two goods. From the results of this study it is recommended that the government equalize the excise rates of the two goods and the Cigarette Tax treatment equation for the two goods.

Keywords: *cigarette; e-cigarette; excise; state levy; tobacco tax; Value Added Ta,.*

INTRODUCTION

The use of all kinds of goods can have an impact on users of goods, the impact arising from the use of an item is called an externality. Externality is a situations where consumption benefits are shared and cannot be limited to particular consumers, or where economic activity results in social costs which or not paid for producer or the consumer who causes them (Musgrave, 1989). There are two externalities, positive externalities and negative externalities. Positive externalities are beneficial effects of the use of the goods. While negative externalities are adverse effects of the use of the goods. Items that cause negative externalities, one of which is cigarettes.

A cigarette is a tobacco product that is intended to be burned and smoked. This includes clove cigarette, white cigarette, cigar, or other forms which produced from plants. The cigarette smoke generally contains nicotine and tar, with or without additives. All contents contained in cigarettes are ingredients that are not good when inserted into the human body. Smoking itself can cause a lot of diseases, such as cancer, pneumonia impotence and reproductive organ diseases, stomach disease, and risk of stroke (depkes.go.id, 2015).

Due to its bad effects, cigarette smoking itself is regulated by the government. The current regulation in Indonesia is The Government Regulation (Peraturan Pemerintah/PP) No. 109 year 2012 concerning Safeguarding Materials Containing Addictive Substances in the Form of Tobacco Products for Health. However, although the government has regulate the rules for the use of tobacco, according to Centre of Excellence for Tobacco Control and Long Health (TCLH), Indonesia was the fourth largest cigarette or tobacco user in the world in 2018 with adult smokers reaching 65,2 millions people. According to the Tobacco Control Support Center (TCSC), smoking trends in Indonesia most often begin from the age of 15 to 19 years, both men and women

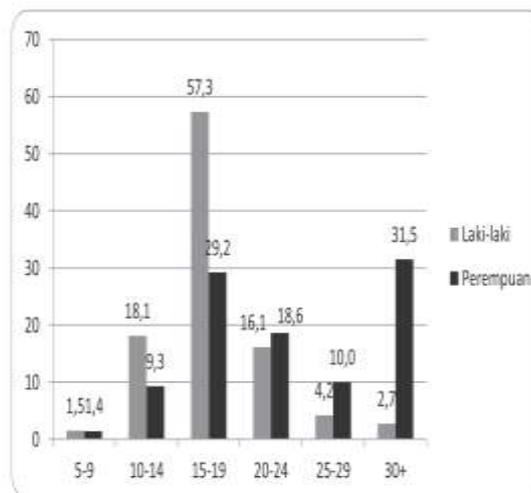


Figure 1. Percentage of Age Starting Smoking in Indonesia.
Source: Tobacco Control Support Center (TCSC), 2014

Based on the 2018 Basic Health Research (Riskesmas) data in Figure 1.2, it can be seen that cigarette consumption from 2007 to 2018 is always high, with the majority smoking, is men rather than women.

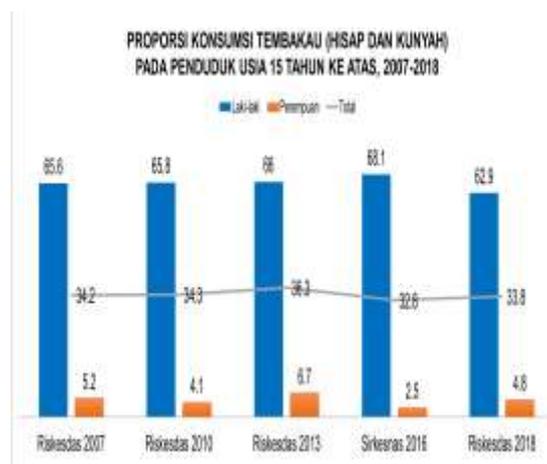


Figure 2. Percentage of Age Starting Smoking in Indonesia.

Over the time, a cigarette transforms into an electric cigarette, e-cigarette or a vape. A vape is one type of nicotine conductor using electronic system. Vape is a device that functions to change chemicals to steam and flow it into lungs using electricity. On its use, a *vape* needs some liquid to produce smoke. This smoke is produced from the vape liquid that is burnt inside the vape machine. The liquid contains some chemical contents such as: Propylene Glycol (PG), Vegetable Glycerin (VG), Flavor, and Nicotine. However, a vape can not be used as an alternative to stop smoking since it still contains some chemical substances which are harmful to our body. Based on the Tobacco Prevention Toolkit by Stanford University, the use of vape can have a negative impact on the body.

The Indonesian Ministry of Health's Research and Development Agency Research Team in 2015 conducted research on junior and senior high school students, totaling 11,031 students in 26 provinces covering 68 cities and a total of 75 junior and senior high schools, found that there were middle and high school students who consumed vape.

Because both of them, cigarettes and vape, are both dangerous if consumed or used, the government urgently needs to regulate the use of these goods. Therefore they are subject to the excise. Excise is a levy made on certain goods which have certain characteristics and characteristics (Ali and Indriani, 2015). These goods and characteristics have a negative impact on human health, stability, order and state security, economic distortions, and their use needs to be limited and monitored. Up to now, cigarette excise rates are regulated in Minister of Finance Regulation (PMK) No. 146/PMK.010/2017 concerning Tobacco Excise Tariffs. Meanwhile for vape, the rule was startly regulated since the government began to realize the increasing of vape consumption in community, including among children. In the level of consumption, some externalities which arised are also as dangerous as externalities of cigarette. As a consequence, the government took some actions to regulate vape use with the excise tax. Due to the fact that there is also tobacco element in a vape, the regulation of vape excise is also using tobacco excise rules. Vape regulation had just arranged in 2017 with the release of Minister of Finance Regulation No. 146/PMK.010/2017. On this Minister of Finance Regulation, a vape is subject to an excise tax at a maximum rate, which is 57% of the HJE. The government, in setting maxium tariffs on vape excise, assumes that vape users come from upper-middle class of society. Vape excise has startly collected since July 2018 and the regulation related to vape excise by the issuance of the Minister of Finance Regulation No. 156/PMK.010/2018 concerning the changes above PMK No. 146/PMK.010/2017. For cigarette excise duty, it is charged per stick or per gram, while for vape, it is applied per ml or per catridge of the liquid vape. In addition, there are some groups in cigarette tax where they are distinguished from HJE, for the highest group is Group I and the lowest is Group III, the higher the group, the higher the HJE, and in vice versa. This tax is levied on the cigarette manufacturers themselves, so that the tax burden imposed by the manufacturers is charged on the price of the cigarette. This happens exactly the same with the vape tax. It is equally charged on the vape liquid price, making it is more expensive. There is some evidence that the excise revenue from tobacco products, especially cigarettes is continually increasing from APBN-P year 2015 up to 2017. These data indicates that cigarette production is always increasing. It shows that the excise tax policy

does not work properly. The excise policy's main goal is supposed to limit the use and control the negative externalities of cigarette, and not to be the source of a country's revenue.

Regarding to the vape excise, some governments have already regulated vape excise. One of them is South Korea. South Korea was the first county in the world which introduce vape or electronic cigarette in 2011 (vaporproductstax.com, 2016). South Korea has taken action to respon the vape phenomena with the same treatment as conventional cigarettes since vape is a modernization of conventional cigarettes. This happens for their same characteristic. Both of them give some negative effects especially on health. Based on table 1.4 above, it can be seen that for vape and cigarette, the South Korean government doesn't use excise only, it also use other elements or levies which can be named as an earmarked tax,

Table 1
Government levies on vape and cigarette in South Korea

Name	Cigarette	Vape
<i>Tobacco Excise Tax</i>	KRW 1007	KRW 628
<i>Local Education Tax</i>	KRW443	KRW 276
<i>National Health Promotion Charge</i>	KRW 841	KRW 525
<i>Waste Charge</i>	KRW 24,4	KRW 24,4
<i>Tobacco Production Stabilization Charge</i>	KRW 5	-
<i>Special Consumption Tax</i>	KRW 594	KRW 370
<i>VAT</i>	KRW 409	-
Total	KRW 3323 (74%)	KRW 1453
Margin	KRW 1177 (26%)	-
Retail Price	KRW 4500	-

Source : World Bank Group, 2018

In Indonesia Cigarettes have been regulated by Indonesian Government which does not only use the excise element. For cigarettes, each province is subject to a Cigarette Tax which is regulated in Law Number 28 of 2009 concerning Regional Taxes and Regional Levies, which is charged at 10% of the Cigarette Excise and this Cigarette Tax revenue is allocated at least 50% for the public health services and law enforcement. In addition to Cigarette Tax, cigarettes in Indonesia are subject to Value Added Tax with rates 9,1 % of other values. Meanwhile, for vape or electric cigarette, so far it is only subject to the excise duty. The trend of vape or electric cigarette use has increased along with its use by tobacco smokers as an altenative to stop regular cigarette smoking. Concerning the increasing of vape use along with the rise of its negative externality on living things and environment, the

government needs to take some action to regulate this problem. Therefore, the government bravely imposed an excise on liquid vape due to the negative externalities, boldly to impose a maximum a maximum excise tax of 57% of its HJE (The Minimum Retail Price). However, the government has not dared to take action to increase the maximum excise tax on cigarette. In fact, these two items, vapes and cigarettes, have obviously created some negative externalities. Unfortunately, there are differences in treatment by the government for these two items. Vapes which still have very few user are subjected to 57% of excise tax, while cigarettes whose users are continue increasing are not subject to maximum excise tax. This paper is analyze the differences in the treatment of state charges on vape and conventional cigarettes.

LITERATURE REVIEW AND HYPOTHESIS DEVELOPMENT

Excise is an selective tax on goods and services, which is defined as a tax imposed on certain goods and services (Cnossen, 2005). According to Cnossen (2005), the main purpose of this tax collection consists of raise revenue for general purposes, reflect external costs, discourage consumption, charge road users for government provided services. The imposition of excisable goods is based on the use of goods which results in externalities. Externalities is when the activity of one entity (a person or a firm) directly affects the welfare of another in a way that is outside of market mechanism, that affect called an externality, because one entity directly affects the welfare of another entity that is external to the market (Rosen,2008).

In the collection of cigarette levy, also subject to value added tax. VAT is a tax on the value added by a firm to its products in the course of its operation. Value added can be viewed either as the difference between a firm's sales and its purchase during an accounting period or as the sum of its wages, profits, rent, interest and other payments not subject to the tax during that period (Rosdiana,2014). Value Added Tax have three advantages fiscal advantages,psychological advantages, and economic advantages.

Cigarette Tax is a tax that is imposed on cigarette consumption. The amount of cigarette tax rates is an important instrument for the government in reducing the level of public consumption of cigarettes. For cigarette tax, two types of tariffs can be applied, namely specific rates and advalorum rates, "The choice between specific and ad valorum taxation therefore depends on whether the primary aim of the policy is to discourage smoking or to raise revenue and on whether improvements in cigarette quality are deemed desirable or not.

RESEARCH METHODS

In this study, the primary data are obtained through field studies, namely in-depth interviews. In-depth interviews are carried out with informants related to the study, including Implementing Section of Regulation in Directorate General of Taxes, Fiscal Policy Agency, Indonesian Personal Vaporizer Association (APVI), Directorate General of Customs and Excise, Regional Tax and Retribution Agency, Consumer Association From Indonesia, Center For Indonesia Taxation Analysis, and Lecturer from Customs and Excise Agency. The informants are given freedom to answer questions according to their opinions since the authors do not limit the answers. Secondary data in this study are obtained through

literature studies, such as books, journals, legislation, scientific studies such as thesis, journals, and other similar data related to the study.

This study applies qualitative data analysis. The data obtained through field studies are coded to produce a concept related to the study. Researcher is using qualitative approach since this study does not intend to measure a matter, but to analyze an event which is the evaluation of a country levies policy on conventional cigarettes and electric cigarettes, where there is a difference in government treatment towards the two kind of cigarettes. It is also to determine the structure of the country levies on both conventional and electric cigarettes.

ANALYSIS AND DISCUSSION

The country's levy is the cost collected by the government from the public for the purpose of the country's revenue. It can be on all types of goods or services. The country's levy on each item or service is different. There are some goods or services that are subject to a single levy. Some of them are subject to several levies at once. Some interesting items to discuss about their levies are conventional cigarettes which have high consumption rates, and also the electric cigarette or vape which becomes a recent trend in community and its industry develops rapidly. There are differences in the Treatment of State Levies on Conventional Cigarettes and Electric Cigarettes. So far, conventional cigarettes have three levies imposed, namely Excise, Value Added Tax, and Cigarette Tax. Meanwhile, for electric cigarettes only have two levies, namely Excise and Value Added Tax.

Conventional cigarettes are subject to excise based on their type and classification . Cigarette which indicated to be an item that needs more health warning based on the Law of Health is a precise subject to excise duty since it is in accordance to the nature and characteristics of the Excisable Goods in the Excise Law. Cigarette in the Excise Law is classified as one of Tobacco Products. For cigarettes made in Indonesia, the basic price uses the Factory Price and Retail Sale Price. As for the imported ones, the basic price uses Customs Value plus Import Duties and retail Sale Price. The excise tax on tobacco products is now regulated further in the Minister of Finance Regulation No.146/PMK.010/2017 concerning Excise Tariffs for tobacco products, and the Minister of Finance Regulation No.156/PMK.010/2018 concerning about the Amendment to the Minister of Finance Regulation No.146/PMK.010/2017.

Concerning Excise Tariffs, electric cigarette excise tax, use ad valorem excise tax, which is 57% of HJE. With the ad valorem tariff system, whatever the proposed price, the excise tax will always be 57% of the price. This is different from conventional cigarettes, where the higher the price, the percentage of excise tax is smaller than the price, while for e-cigarettes the percentage of excise tax will always be 57%. According the difference in the tariff system is more directed to its objectives. The specific tariff system is more aimed at optimizing excise revenue and legal certainty to avoid tax avoidance. Legal certainty because of the excise it is clear how much is left just to adjust the tobacco products into which class, so that the excise itself is clear because it is based on class. It can be said that with a specific excise tax system it is difficult to avoid taxation, because it is clear how much excise tax must be collected. However, this specific rate must continue to be adjusted so that inflation is not eroded. Meanwhile, the ad valorem tariff system is more aimed at

justice, because each tobacco product is subject to the same tariff and also the amount is adjusted based on its own price. The advalorem tariff system does not depend on the price of tobacco products, because as prices change, this tariff will adjust how much is levied from the price.

In addition to excise instruments, the government also regulates conventional cigarette using other instruments, namely the tax instruments. The government imposes a tax on conventional cigarettes consisting of two taxes: National Tax and Regional Tax. For the National Taxes, the government imposes the Value Added Tax (VAT) on tobacco products. VAT is a tax that is levied on the supply of Taxable Goods and Taxable Services within the customs area. This VAT is generally applied to all delivery of goods and services, so this tobacco product is included in the VAT object. However, VAT for tobacco product is regulated by specific ministerial rules. Recently, the Tobacco Product VAT is regulated in the Minister of Finance Regulation. The basis for taxation of Tobacco Product VAT uses the "Other Value", where the "Other Value" is based on The Minister of Finance Regulation Article 3 Paragraph 2 No.174/2015 that consist of:

- Retail Sale Price of Tobacco Products for delivery of Tobacco Products, or
- Retail Price of Tobacco Products for the same type and brand, which is sold to the public after deducting the gross profit for the free delivery of Tobacco Products.

Tobacco Product VAT is imposed at one level on producer and/ or importer level. The VAT is payable when the producer and/ or importer orders the tobacco excise. Tobacco Product VAT is levied on the delivery of tobacco products by calculating the effective rate multiplied by "Other Values". Effective rate is the rate applied to calculate and collect VAT that is levied on the delivery of tobacco products. In addition to National Tax, cigarette is also subject to local tax. Regional taxes are mandatory contributions to regions owed by individuals or entities that are enforceable under the law, with no direct compensation and are used for regional prosperity. Cigarette Tax or excise is levied by the local government. According Regional Tax and Levy Law, the cigarette tax object is the consumption consumption of cigarette in general including cigarette, cigar, and leaf cigarette. The cigarette tax subject is the consumer of cigarette. Meanwhile, cigarette taxpayers are cigarette producers and importers who have licenses in the form of excisable goods company registration number. The cigarette tax is levied by the local government which has the authority to collect the excise duty along with cigarette tax collection. This government authority is Directorate General of Customs and Excise.

The second difference is for the cigarette tax. So far, cigarettes are subject to cigarette tax, namely only three types, cigarettes, cigars, and leaf cigarettes. The cigarette tax is still new because it was only regulated in 2014, and the condition was that at that time the e-cigarette was not regulated. The cigarette tax collected is deposited to Provincial General Cash Account then distributed proportionally based on the population of each region. The cigarette tax tariff which was set by Regional Tax and Levy Law is 10% of the Tax Imposition Base. The Tax Imposition Base is namely Cigarette Tax. The Cigarette Tax Receipts under the Regional Tax and Levy Law must be allocated at least 50% to fund public health services and law enforcement by the authorities.

The Regional Tax and Levy Law constitutes the basis or the reference for each region to regulate Regional Tax, which further regulates and implements the Regional Government re-regulates by issuing regional regulations. The objects and subjects of the cigarette tax are cigarette consumption and cigarette consumers, which include cigarettes, cigars, and leaf cigarettes. Cigarette Taxpayers are cigarette manufacturers and cigarette importers who have a permit in the form of NPPBKC. Cigarette tax rate is the same as stipulated by the regional Tax and Levy Law which is 10%. It is obvious that this cigarette tax is an *Earmarking Tax*, in which the purpose of the collection is to be allocated to certain fields such as health services and law enforcement.

CONCLUSION

The state levies imposed on conventional cigarettes consist of three levies. The first levy is excise. Excise is levied with the aim of controlling cigarette consumption. Cigarette excise tax is currently regulated in PMK No.146 / 2017 concerning Tobacco Excise Tariff. Cigarette excise rates vary depending on the type, currently the highest tariff is around 55.3% of HJE, or as much as Rp. 625 from the minimum HJE of Rp. 1,130 for Class I SPM cigarettes. The second levy is the Tobacco Value Added Tax. Tobacco Product VAT is collected because of the delivery of Excisable Goods, namely Tobacco Products, one of which is cigarettes. Tobacco Product VAT is regulated in PMK No. 174/2015 concerning Tobacco Product VAT, and subject to an effective tariff of 9.1% of Other Value. The third levy is the cigarette tax. Cigarette Tax is a local tax that is imposed on cigarette consumption. DKI Jakarta Cigarette Tax is regulated in Perda No. 2/2014 regarding Cigarette Tax, with a rate of 10% of the cigarette excise tax. From the state levies on cigarettes and electric cigarettes, there are two different treatments. The first difference is the difference in tax treatment. So far, cigarettes have not been subject to a maximum excise tax rate, while electric cigarettes were first set directly subject to maximum rates. This is due to protect the cigarette industry, because the existence of electric cigarettes is now a new competitor from the cigarette industry. Conventional cigarettes have labor issues, if the industry is disrupted it will have social and economic impacts on workers in the cigarette industry. In addition, the imposition of maximum rates for e-cigarettes aims to equalize the levies on conventional cigarettes, because conventional cigarettes when combined can reach 70%, so that the total amount of e-cigarette levies needs to be synchronized with conventional cigarettes by imposing a maximum tax rate on e-cigarettes. The second difference is the difference in cigarette tax treatment. The cigarette tax so far only regulates cigarettes, cigars and leaf cigarettes, while e-cigarettes are not included in the definition of cigarettes.

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