



POLICY BRIEF:

Institute of Policy Studies of Sri Lanka

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Importance of Effective Alcohol Taxation in Sri Lanka

Introduction

Non-Communicable Diseases (NCDs) are a main health burden, accounting for 36% of healthcare spending and constituting the leading cause of hospital deaths in the country (accounting for 83% of deaths).^{1,2} This growing concern is evidenced by around 100,000 premature deaths annually attributed to NCDs.³ The key to tackling this issue is preventing NCDs, primarily by addressing common risk factors. By promoting the reduction of practices such as tobacco use, alcohol consumption, physical inactivity, and the consumption of unhealthy diets, the nation can take substantial strides towards curbing the impact of NCDs on public health.

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Policy Options

Policies that help to arrest NCD risk factors, such as smoking and alcohol use would be effective. Global research and country experiences have shown that increasing the price of alcoholic beverages through taxation is one of the most cost-effective policies to lower drinking levels and alcohol-attributable harm. This has been recognised as a “best buy” intervention by the World Health Organization (WHO), delivering greater health impacts in reducing illness, disability and premature death than other policy options.

Following global recommended practices, the Sri Lankan government employs alcohol excise tax method (involves applying taxes based on the alcohol content of alcoholic beverages) to reduce consumption and generate revenue. To combat excise duty evasion, a foolproof liquor sticker has been made obligatory on domestically produced alcohol starting from April 1, 2022. In a recent update, the Excise Department reported the discovery of more than 44,000 liquor bottles bearing fraudulent

1 Directorate of Non-Communicable Diseases Ministry of Health, *Annual Report 2021*, Ministry of Health.

2 World Bank. (2019). Retrieved January 20, 2023, from World Bank Indicators: <https://data.worldbank.org/indicator/SH.DTH.NCOM.ZS?locations=LK>

3 World Health Organization. (2020). *Global health estimates 2020: Deaths by Cause, Age, Sex, by Country and by Region, 2000-2019*. Geneva, World Health Organization.

stickers during their inspections at 52 alcohol bottle production sites.⁴ Each liquor bottle with a counterfeit sticker resulted in a substantial loss of Sri Lankan Rupees (LKR) 2,900 in tax revenue for the country. The counterfeit liquor stickers have cost Sri Lanka a staggering LKR 1.2 billion (Bn) in tax revenue.

Alcohol excise taxes have received media attention recently as a result of the loss of tax income brought on by incorrect implementation of tax collection. **To combat this problem effectively, the government should strengthen law enforcement pertaining to illicit trade control** -- encompassing increased enforcement raid operations and introducing mobile application-based QR tracking system. Failure to do so would entail higher government expenditures on socio-economic consequences associated with alcohol, surpassing the revenue generated from alcohol excise duties.

Background

The escalating prevalence of NCDs compounds the burden on the healthcare sector, straining resources and budgets. According to the official data, health expenditure already constitutes 7.1% of the total government expenditure.⁵ Moreover, the fiscal toll of NCDs becomes even more apparent when considering specific factors. As of 2015, the economic and social costs of alcohol consumption

alone amounted to a staggering LKR 119.66 Bn for the government.⁶

This sum equates to a substantial 8.2% of government revenue for the same year, underscoring NCDs' financial implications for the government's fiscal burden.⁷ Moreover, the fiscal toll of alcohol use was even higher than the government revenue earned from alcohol excise taxes in the same year, which was LKR 105.23 Bn.⁸

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Efforts to control alcohol consumption in Sri Lanka are warranted, given the prevalence and variety of alcohol usage. Based on the Household Income and Expenditure Survey (HIES) 2019 data, around 9% of households in the country consume alcohol. A significant portion of alcohol consumers, 73%, opt for arrack, while around 18% opt for beer (see Table 1). Further, traditional alcoholic beverages is low around 6% of alcohol user households use toddy and around 6% use Kasippu.

The type of alcoholic beverage consumed often exhibits regional variations, with a clear divide between urban and rural settings. Traditional alcoholic beverages find greater favor in rural and estate sectors (see Table 2).

4 Daily Mirror. (2023, September 09). *Counterfeit liquor stickers cost Sri Lanka Rs. 1.2 Billion in Tax Revenue*. Retrieved September 10, 2023, from Daily Mirror: <https://www.dailymirror.lk/front-page/Counterfeit-liquor-stickers-cost-Sri-Lanka-Rs-1-2-Billion-in-Tax-Revenue/238-266933>

5 Central bank of Sri Lanka. (2022). Annual Report. Colombo: Central bank of Sri Lanka.

6 World Health Organization. (2017). Economic and Social Cost of Tobacco and Alcohol in Sri Lanka - 2015. World Health Organization- Country office for Sri Lanka.

7 Central bank of Sri Lanka. (2016). Annual Report. Colombo: Central bank of Sri Lanka.

8 Ministry of Finance. (2016). Annual Report 2016. Colombo: Ministry of Finance.

For instance, toddy is more prevalent in the estate sector, reflecting its cultural significance in these areas. In contrast, Kassippu, a locally brewed spirit, is predominantly consumed in the rural sector, showcasing the diversity in alcohol consumption patterns across different regions.

These statistics emphasise the need for comprehensive alcohol control measures to address the diverse patterns of consumption and their potential impacts on public health, social well-being, and economic stability.

Table 1 : Household Level Alcohol Consumption

Alcoholic beverage	Monthly expenditure on alcohol	Number of alcohol consuming HHs	As a % of alcohol user HHs
Arrack	5,862	362,456	73
Beer/Stout	3,441	91,233	18
Toddy	2,655	28,104	6
Kasippu	4,592	31,516	6
Whisky/Brandy	16,220	12,094	2
Gin	2,781	1,106	0
Wine	4,482	950	0
Other alcohol	7,876	4,900	1
All alcohol	5,868	494,270	

Source : Constructed based on HIES 2019

Table 2 : Type of Alcohol Users by Region

Sector	Number of alcohol consumer households					
	Alcohol	Arrack	Beer	Toddy	Kasippu	Other liquor
Urban	82,294	54,393	23,960	1,791	2,532	5,698
Rural	346,299	252,632	61,733	20,011	26,466	12,729
Estate	65,676	55,431	5,540	6,301	2,518	229

Source : Constructed based on HIES 2019

The financial burden of alcohol consumption is evident in the expenditures of households. On average, households where alcohol is consumed, allocate a substantial portion of their budget to alcohol, with a monthly spending of almost LKR 6,000 (see Table 3). This significant expense translates to about 8% of the household's overall budget, thus driving out other critical expenditures – education, health, and housing. Addressing the economic implications of alcohol spending is crucial, not only for individual households but also for the broader economic stability of the country.

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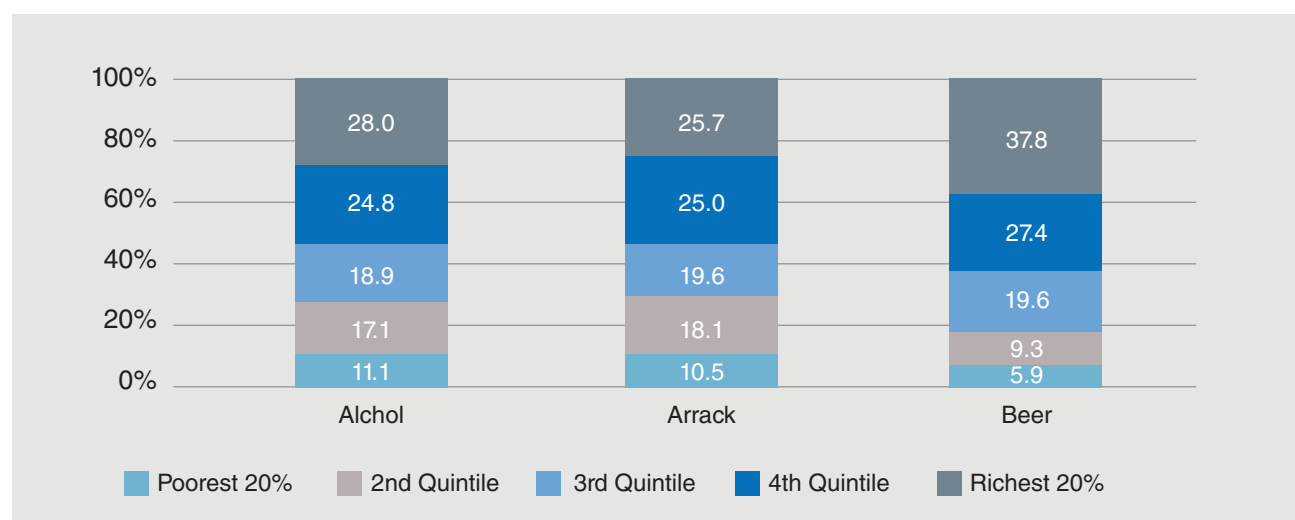
Alcohol taxation emerges as a favourable policy option, considering the distribution of alcohol consumption across different household income levels. A significant portion of alcohol consumers originates from more affluent households. For instance, around 50% of arrack and 65% of beer consumers belong to the top 40% wealthier segment (Figure 1).

Table 3: Spending on Alcohol

Household (HH) expenditure group	Average monthly alcoholic beverage expenditure (LKR)						Budget share of spending		
	Alcohol	Arrack	Beer	Toddy	Kasippu	Other liquor	Alcohol	Health	Education
Poorest 20%	3,306	2,375	346	278	188	119	10.1	0.9	2.2
2nd Quintile	3,945	3,107	219	268	331	19	9.6	0.9	3.1
3rd Quintile	4,919	3,999	458	154	298	11	10.1	1.6	3.1
4th Quintile	6,193	5,103	669	105	266	50	9.8	1.6	3.2
Richest 20%	8,417	5,284	1,095	67	331	1,640	6.1	2.1	4.1
All	5,868	4,299	635	151	293	490	7.9	1.7	3.6

Source : Constructed based on HIES 2019

Figure 1: Distribution of Alcohol Users by Income Groups



Note : Due to small sample sizes, quintile breakdowns are not given for Toddy and Kasippu.

Source : Constructed based on HIES 2019

Benefits of increasing alcohol tax:

Alcohol excise taxes can effectively curb alcohol consumption, leading to numerous advantages.

Alcohol excise taxes offer a two-fold advantage, presenting positive outcomes for both government revenue and public health:

- **Increased Government Revenue:** One of the significant benefits of implementing higher alcohol excise taxes is the boost in government revenue. This additional income can be directed towards vital sectors such as healthcare, potentially alleviating some of the financial burden faced by the health sector. Further, diminishing the prevalence of alcohol consumption will decrease productivity losses attributed to work absenteeism.
- **Reduction in NCD risks and health costs:** Implementing higher alcohol taxes is a powerful tool to mitigate the risks associated with NCDs. By raising the cost of alcohol, it becomes less affordable, leading to a decrease in alcohol consumption. This reduction in consumption contributes to a decline in the adverse health consequences of alcohol use. This, in turn, eases the strain on the healthcare system by lessening the burden of treating alcohol-related health issues. Lowering the incidence of NCDs translates to reduced healthcare costs in the long run.

This strategy has the potential to not only enhance public health outcomes but also positively influence household finances and overall well-being. Such a tax increase garners broad public support as it does not impact essential goods.

Conclusion

These insights underscore the potential effectiveness of alcohol taxation as a means to reduce consumption and generate revenue, particularly given its potential to target a more financially capable population segment. Furthermore, given that economically disadvantaged groups are more prone to price changes and reduce their consumption, increasing the price would have a progressive effect. Such a policy could address the health and economic challenges of alcohol consumption in Sri Lanka. In summary, implementing higher alcohol excise taxes holds the dual promise of bolstering government revenue and fostering improved public health.

Moreover, to offset the expenses associated with alcohol-related issues, it is vital to uphold effective alcohol tax rates while simultaneously mitigating potential revenue losses resulting from the illicit alcohol market. Therefore, it is essential to enforce stringent regulations to penalise alcohol manufacturers (if the counterfeit labels continues), thereby maintaining control over illegal alcohol products entering the market.

Additionally, efforts to improve efficiency and transparency involve conducting swift and targeted raids on individuals suspected of participating in this unlawful activity, leveraging QR technology could mitigate tax evasion.