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The Power of Indirect Taxation: How Governments use Fiscal Tools to Shape Markets and Choices

PIVOT.

Introduction

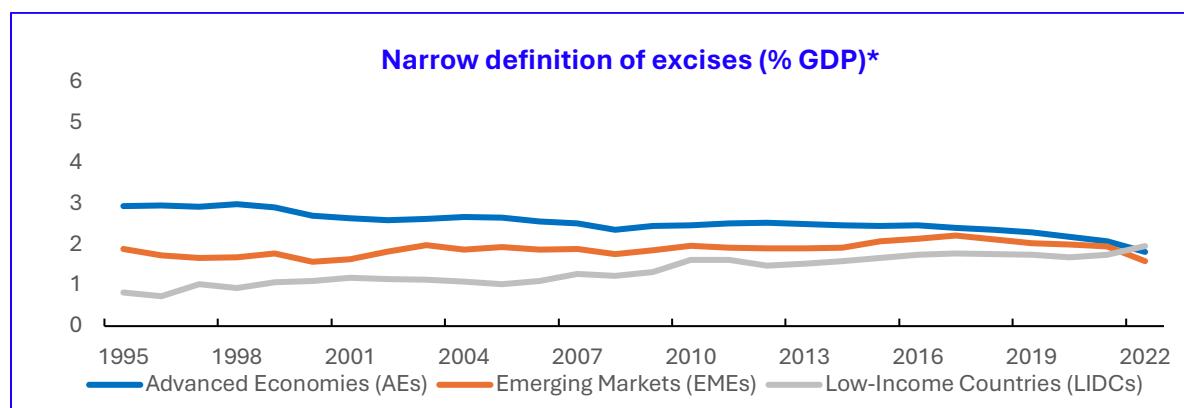
In an era marked by economic uncertainty and fiscal constraints, governments are increasingly turning to indirect fiscal tools, such as excise duties and behavioral levies. These levies not only to raise revenue but also to shape markets and embed public priorities like health and sustainability into economic systems. At the **seminar hosted by Pivot at the IFA Congress in Lisbon**, leading experts explored how forward-looking tax policies can strengthen fiscal resilience and guide both consumer and business behavior, drawing on comparative evidence and country case studies.

Indirect Taxation: Design, Impact, and Equity

Indirect taxes, particularly excise duties and behavioral levies (e.g., taxes on sugar-sweetened beverages and tobacco), have become central to modern fiscal policy. While their primary purpose has traditionally been revenue generation, these instruments are now deployed as strategic levers to steer consumption, support long-term industrial development, and manage external shocks.

A comprehensive analysis of tax design reveals the nuanced impact of these policies on consumer behavior. The seminar's panelists placed particular emphasis on tobacco taxation, a domain where the regressive nature of excise taxation is especially pronounced. Lower-income consumers often bear a proportionally higher financial burden, raising important questions regarding equity and social impacts.

Global trends show that excise tax revenues as a share of GDP have converged to 2–3% across advanced and emerging economies, a significant decrease from higher levels in the early 1990s. This decline might be partly explained by a lack of indexation (i.e., the adjustment of tax rates in line with inflationary trends) and the slow adaptation of tax systems to new products and alternatives. (Source: IMF World Revenue Longitudinal Database, 2025)



*The narrow definition of excise taxes refers exclusively to classic excise goods, such as alcohol, tobacco and fuel.

Panel Insights: Lessons from Practice

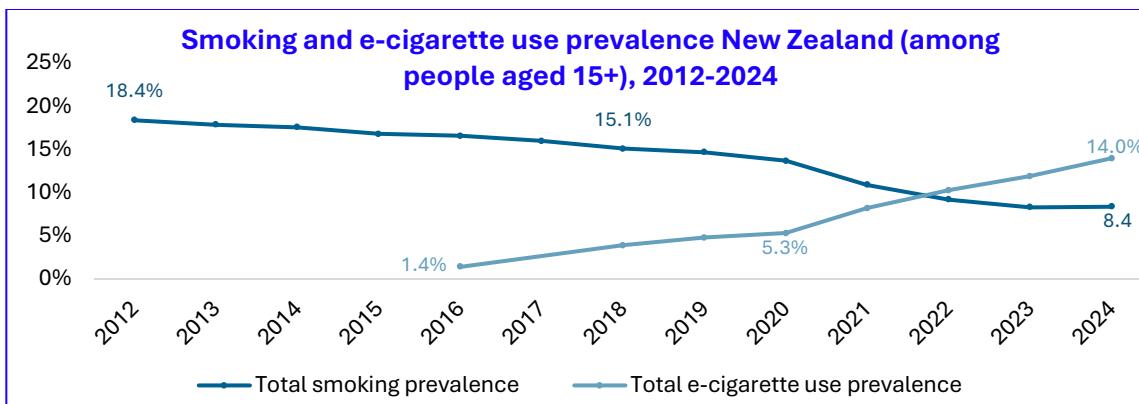
Mario Mansour (International Monetary Fund) emphasized the significance of thoughtful tax design and the need for understanding elasticities. He pointed out that raising prices generally leads to lower consumption and helps address negative externalities. Excise taxes, in his view, are not solely designed to generate revenue but also to gradually reduce the size of the taxed market. He identified several factors crucial to the success of corrective taxes: clear policy objectives, a wide tax base, consumer demand that does not change drastically in response to price shifts, and credible enforcement mechanisms.

Philip Barry (TDB Advisory) highlighted how excise taxation influences consumption patterns, drawing on New Zealand's experience. He illustrated that indexation and thoughtful, long-term policy planning play a crucial role in ensuring sustained effectiveness. According to Barry, predictable and multi-year tax strategies tend to be more successful than those implemented on an ad hoc basis, as they better promote targeted outcomes, strengthen government revenues, and decrease volatility. He also noted that supporting regulations and policies are necessary to preserve both revenue streams and policy effectiveness over time.

Ashok Kaul (Roland Berger N3XT) underscored the value of providing alternatives as vital incentives for reducing externalities. He argued consumers must be offered healthier and less harmful options to encourage shifts in behavior, pointing to the success of risk-based regimes that incentivize the adoption of reduced-risk products.

Case Studies: Tobacco Excise Policy in New Zealand and Australia

New Zealand adopted a risk-based excise tax regime targeting a $\leq 5\%$ smoking prevalence by 2025. Tobacco excise tax rates increased annually by 10% plus inflation indexation from 2010 to 2020, with reduced rates for lower-risk alternatives. Smoking prevalence fell from 18.4% (2012) to 8.4% (2024), while the use of reduced-harm e-cigarettes rose to 14%. Government revenue from tobacco excise taxation continued to grow until around 2020, then declined as smoking rates dropped, a sign of successful policy implementation.

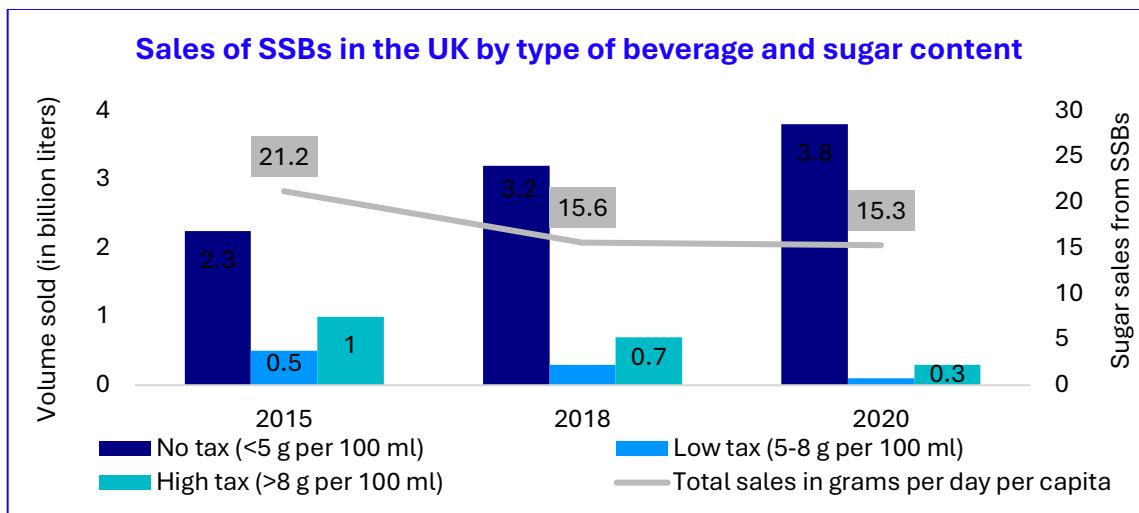


Australia followed a similar approach, with annual excise increases and additional surcharges. Smoking prevalence fell from 15.0% (2013) to 10.0% (2023), and government revenues remained strong until about 2020 before declining. Both countries' experiences highlight the importance of long-term planning, indexation, and the provision of product alternatives.

Behavioral Taxes as Economic Levers

The seminar also explored the broader application of behavioral taxes as economic levers for health and sustainability. Examples included:

- **The UK's Soft Drinks Industry Levy** introduced a tiered excise tax structure based on sugar content. Since its implementation in 2018, the proportion of soft drinks with high sugar content has declined by over 30%, and per capita sugar sales in soft drinks have decreased by approximately 30%. (Source: Public Health England, 2022)
- **Ireland's Plastic Bag Environmental Levy**, which reduced the percentage of plastic bags in total waste from over 5% in 2001 to approximately 0.13% in 2014, while generating over €200 million in revenue between 2002 and 2013. (Source: Green Budget Europe, 2016)
- **The EU Commission's proposal for tobacco and nicotine taxation** which introduces risk-proportionate tax rates aligned with each product's health risk profile, incentivizing industry transformation toward reduced-risk alternatives.



These case studies illustrate how well-designed behavioral taxes can steer both consumer and producer choices toward public health and environmental goals, while also supporting fiscal resilience.

Conclusions and Recommendations

Indirect taxes remain a vital and reliable revenue source in economically challenging times. The seminar's discussions underscored several key recommendations for policymakers:

- **Adopt multi-year planning and indexation** to ensure revenue stability and policy effectiveness.
- **Design risk-proportionate tax frameworks** that align fiscal incentives with public health and environmental goals.
- **Provide alternatives** to encourage behavioral change and reduce externalities.
- **Integrate fiscal and regulatory policy** for maximum impact.

By leveraging indirect taxation as a strategic tool, governments can not only strengthen fiscal resilience but also shape markets and choices in ways that advance public priorities.

References

1. IMF World Revenue Longitudinal Database (2025)
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3. Smokefree New Zealand (2024). [Smoking rates and figures](#).
4. Public Health England (2022). [Sugar Reduction Programme: Industry Progress 2015 to 2020](#).
5. Green Budget Europe (2016). [The Plastic Bag Levy in Ireland](#).
6. European Commission (2025). [Revision of the Tobacco Taxation Directive](#).