Tobacco Europe position on the Tobacco Excise Directive review (Directive 2011/64/EU)

Tobacco Europe AISBL[1] represents the common views of major European–based tobacco and nicotine products manufacturers which includes British American Tobacco (BAT), Imperial Brands (IMB), and Japan Tobacco International (JTI).

Executive Summary

Tobacco Europe takes note of the proposal from the European Commission on the revision of the Tobacco Excise Directive. Tobacco Europe especially appreciates the enlarged harmonisation of tobacco and non-tobacco products with separate and dedicated categories for electronic cigarettes, tobacco-free nicotine pouches (modern oral) and Heated Tobacco Products that have been created.

The rates proposed by the Commission for combustible tobacco products and tobacco related products are too high and are not supported by any evidence. The additional revenues estimated by the Commission are overstated and will not be achieved if the increases go ahead as planned.

Therefore, Tobacco Europe suggests more moderate increases in the minimum rates for all products and a different approach to the taxation of e-liquids.

1. <u>The proposed minimum excise increases on traditional tobacco products are excessive, particularly for Eastern European Member States</u>

   Tax policy remains a sovereign issue for individual Member States and therefore excise rate or excise incidence differences are to be expected across the EU, in the same way that VAT rates differ across EU Member States. Tax differentials (either in Euros or as a percentage of the retail price) are the result of differences in income levels, the cost of inputs and varying economic conditions across Member States.

   The Commission has suggested that the proposed increase in the minimum rates would generate EUR9.4bn in additional revenue. However, this calculation is based on an EU average price elasticity of -0.54 which is wrong. Economisti Associati, the consultants who prepared the study on the rates for the Commission have themselves suggested that PED for cigarettes in the EU is between -0.96 and -1.09, which is much higher than the numbers used by the Commission. This means that the estimated additional revenue will not be achieved.

   The Commission has also suggested that an increase in the minimum rates is necessary to *"reduce the distortive effects on competition of tax-induced cross-border flows of products and contribute to the smooth functioning of the Single Market."* However, cross-border differences in cigarette prices and taxes are similar to those for all consumer goods and services and are therefore not a signal that the Single Market is working ineffectively in respect of these products. Cross-border flows between EU MS only represent around 5% of all cigarettes consumed in the EU. Moreover, the 21.9 bn of cross-border cigarette flows between Member States is almost a third smaller than the 31 billion cigarettes consumed in the EU that were either brought in from non-EU countries or manufactured illegally within the EU, together representing more than 7% of the cigarettes

[1] https://www.tobacco-europe.eu/

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EU Transparency Register: 1496873833-97
Registered number: 089 438 919

consumed in the EU. A large increase in the minimum excise on cigarettes risks exacerbating the consumption of illicit cigarettes across the Single Market.

For these reasons, the minimum rates for cigarettes should be set no higher than 130 €/000. This increase would still require substantial excise rate increases in some Member States.

The Commission also proposes to increase the minimum incidence from 60% to 63% of the WAP with the escape clause[2] will be set at 230 €/000. Since there is no clear relationship between the excise incidence and the excise burden on cigarettes, the minimum excise incidence requirement has not clearly contributed to a convergence in cigarette excise rates across the EU. There should be no change to the minimum rate (i.e. 60% of the cigarette WAP) to avoid disproportionately impacting the excise rates in Member States where cigarettes are already significantly less affordable for consumers. The 'escape clause' threshold must be retained and needs to be set at 155 € /000. This would avoid a disproportionate reduction in tax revenues in several markets where cigarette tax rates are already beyond their revenue maximising rates.

The minimum rates for fine-cut tobacco intended for the rolling of cigarettes should be differentiated from the minimum rate on cigarettes with nominal rates set lower than the minimum rates on Cigarettes but higher than on Heated Tobacco Products in recognition of the distinctive characteristics of fine-cut tobacco.

2. Harmonizing the definitions and tax treatment of tobacco and non-tobacco related products: Heated Tobacco Products, E-cigarettes, Tobacco-Free Oral Nicotine Pouches (Modern Oral)

   Tobacco Europe welcomes the Commission's proposal to harmonise the taxation of novel products with the creation of separate and dedicated excise categories for electronic cigarettes, tobacco-free oral nicotine pouches and heated tobacco products, underpinned by unambiguous definitions. Clear definitions are essential.

   Our more detailed views on the specific excise categories proposed:

   i. The tax levels for Heated Tobacco Products should be set at no higher than 50% of the level for cigarettes. This means that if the minimum rates for cigarettes are set at 130 €/000, the minimum rates for Heated Tobacco Products should be set at 65 €/000 when presented in a stick format. If products are presented in any other format, the rate should be per kilogram. There should only be a minimum tax in monetary terms and no relative rate.
   ii. For e-cigarettes which do not contain tobacco and which may or may not contain nicotine, the minimum rate should not be set with reference to nicotine content as this would be complex to administer and lead to increased levels of tax evasion. A more appropriate solution to address tax evasion is by introducing a differential approach to closed and open systems – which are the 2 categories identified in the Tobacco Products Directive - 2014/40/EU (TPD). Closed systems should have an excise rate set per unit. This rate should be set at 0.2 €/item (with an item being a single cartridge or tank containing liquids or solutions not exceeding a volume of 2 ml as defined in the TPD). For open systems, the rate should be set per ml and should be no less than 0.3 €/ml. The suggested approach is consistent with the proposal for Tobacco Heated Products and what is already common practice between cigarettes and fine cut tobacco for the rolling of cigarettes where cigarettes have a unit tax and fine cut has a tax per weight.

[2] The level at which the 60% incidence requirement does not need to be met.

iii. Oral nicotine pouches which do not contain tobacco should be taxed at lower levels than the rates proposed: the minimum rate should be 20 €/kg. There should only be a minimum level in nominal terms.

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