



*European Commission*

# Taxation of tobacco products in the European Union

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# Legislation on taxation

- *Directive 92/79/EEC* (Approximation of taxes on cigarettes)
- *Directive 92/80/EEC* (Approximation of taxes on manufactured tobacco other than cigarettes)
- *Directive 95/59/EEC* (Taxes other than turnover taxes which affect the consumption of manufactured tobacco)

*Codification of the three Directives is in preparation*

# Main objectives of legislation

- Improve the operation of the internal market:
  - Establish minimum excise duties
  - Approximate the structure of excise duties
- Prevent distortion of competition between different tobacco products
- Safeguard free determination of the maximum retail selling price

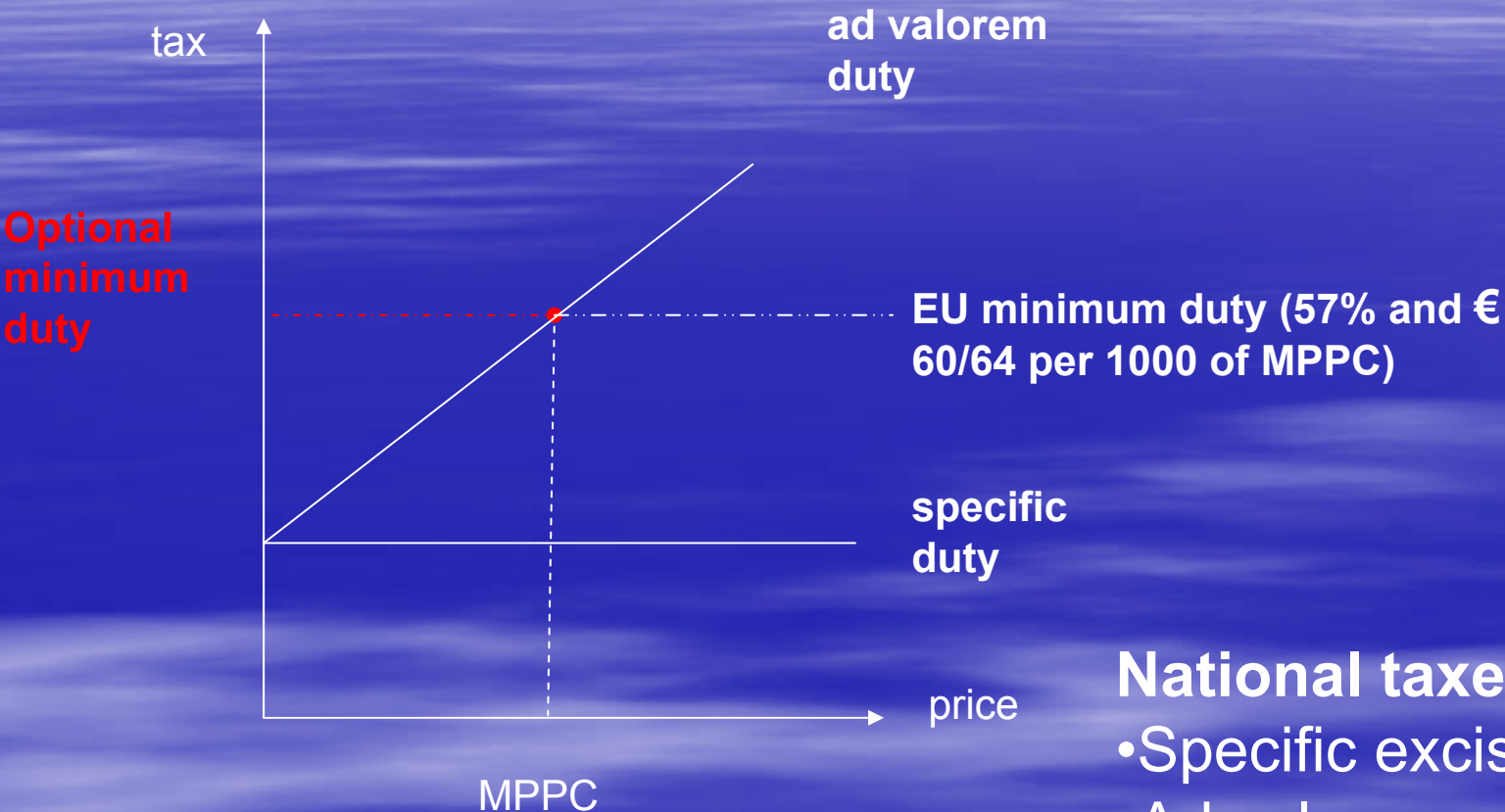
**NB No health policy objectives!**

# Tobacco product categories

- **Cigarettes (majority of market)**
- Cigars and Cigarillos
- Smoking tobacco
  - Fine-cut tobacco for the rolling of cigarettes
  - other smoking tobacco

# Taxation of Cigarettes

# Structure of excise duties



## National taxes:

- Specific excise duty
- Ad valorem excise duty
- VAT

**MPPC – Most Popular Price Category**



# Characteristics of EU taxation system of cigarettes

- Combination of **ad valorem** and **specific duty**
  - Compromise between southern MS (producing raw tobacco and preferring ad valorem taxation) and northern MS (not producing raw tobacco and preferring specific duty)
  - National brands of southern MS are produced with their own, cheaper, national tobacco. Ad valorem system favors these products over cigarettes of international brands, produced with more expensive tobacco

# Taxation structure on cigarettes

- Excise duty on cigarettes must consist of a SPECIFIC and an AD VALOREM element
  - Specific:
    - A fixed amount per 1000 cigarettes
    - between 5% and 55% of total tax (excise + VAT)
  - Ad valorem:
    - A percentage of **Tax Inclusive Retail Selling Price (TIRSP)**
  - The specific amount and the ad valorem % are applied to cigarettes of all price categories



# Minimum overall excise duty on cigarettes

- **Minimum level of taxation**
  - 57% of the TIRSP of cigarettes and
  - € 60 per 1000 cigarettes (€ 64 from 1/07/2006)
  - **Both established by reference to MPPC (Most Popular Price Category)**

# Derogations and transition periods

- MS with minimum excise duty of at least € 95/1000 (€ 101/1000 since 1/07/2006) for MPPC do not need to comply with 57% rule (Sweden, Denmark)
- Transition period for Greece and Spain: € 64 have to be reached by 1/1/2008 (though currently Greece has € 78/1000 and Spain € 69/1000)
- Transition periods for the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Slovakia and Slovenia: € 64 have to be reached by 31/12/2007 – 31/12/2009
- Transition period for France: lower excise duties can be levied to cigarettes for Corsica until 31/12/2009

# Optional minimum excise duty

- Legal basis
  - Article 16(5) of 95/59/EEC (cigarettes)
- Requirements:
  - Applied to cigarettes sold at price lower than MPPC
  - Cannot exceed the excise duty levied on MPPC
- 17 MS introduced a minimum excise duty on cigarettes

# Example (pack of 20)

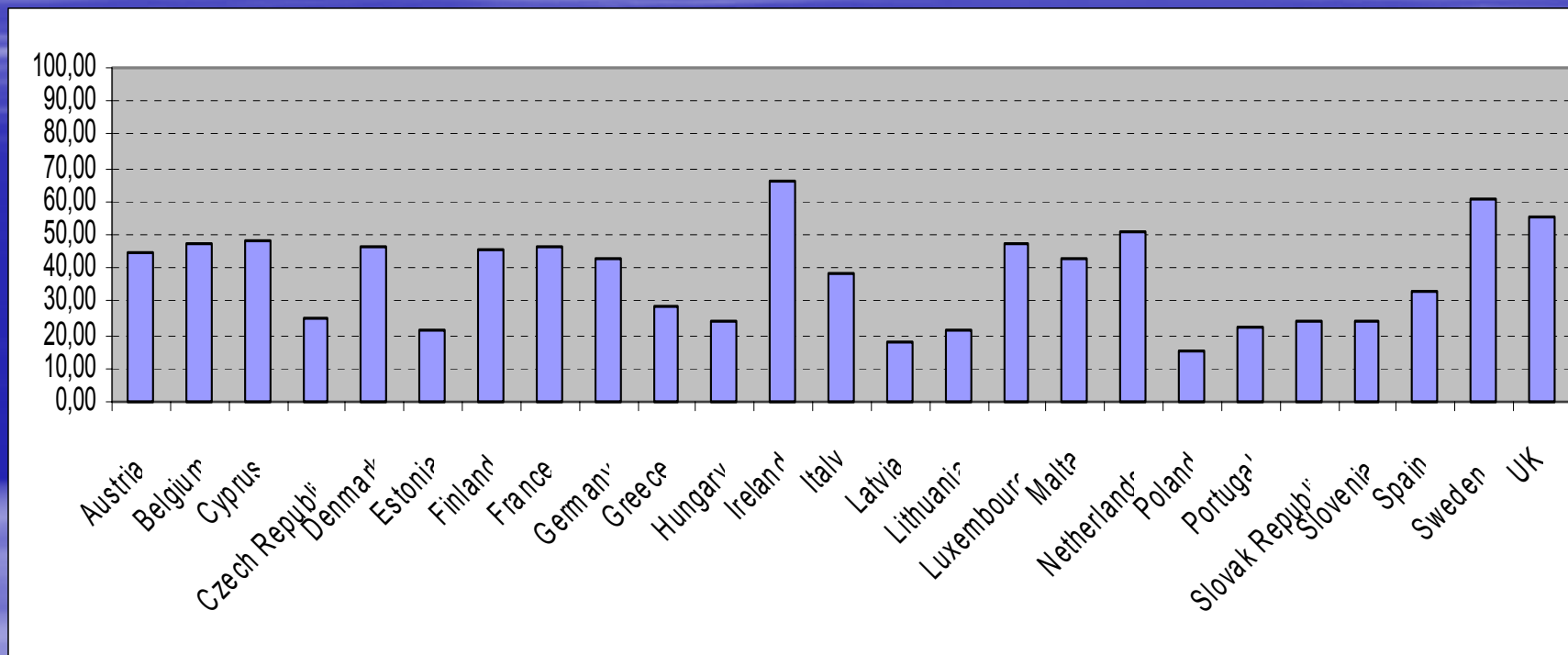
Pre tax price (excluding taxes)	0.7	EUR
TIRSP		EUR
Excise duty		
- <i>Specific:</i>	1 EUR	
- <i>Ad valorem:</i>	0.8 EUR (27% of TIRSP)	
- <i>Total:</i>	1.8	EUR (60% of TIRSP)
Price excluding VAT	<u>2.5</u>	EUR
VAT 20%	0.5	EUR
TIRSP (including taxes)	<u>3</u>	EUR

Notes: - Total tax (excise + VAT) = 2.3 EUR or 77% of TIRSP

# Tax and TIRSP differentials in MS (I)

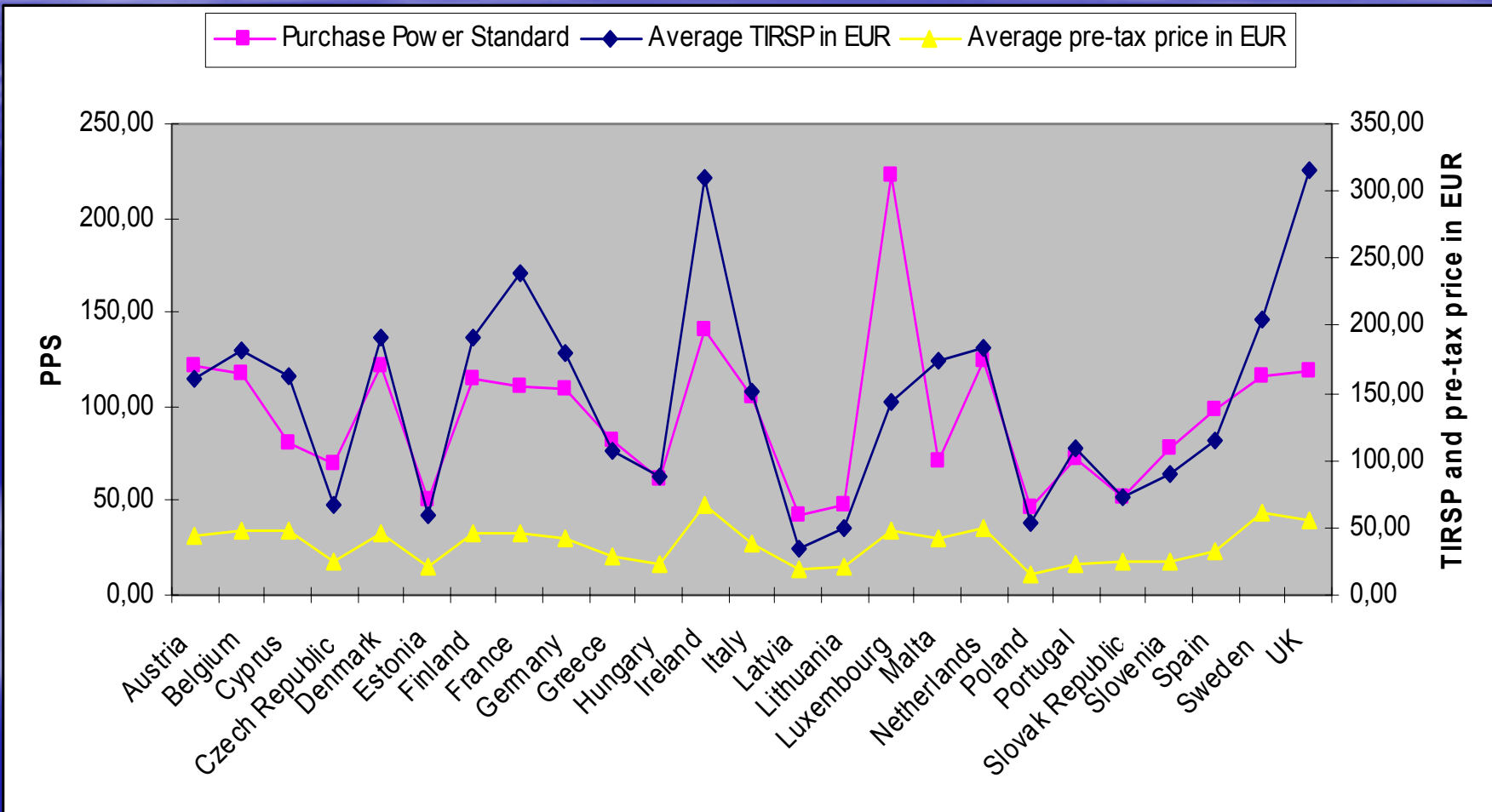
- After the enlargement, the differentials have widened (EU15: 1/4, EU25: 1/7)
- Resulting from differences in:
  - Pre-tax prices (depending on purchasing power) and retail margins
  - Excise duty rates
  - Structure of excise duties
  - VAT (15-25%) on tobacco products (multiplier effect)

# Average pre-tax prices in 2004 in EUR/1000





# Relationship between PPS, pre-tax prices and TIRSP



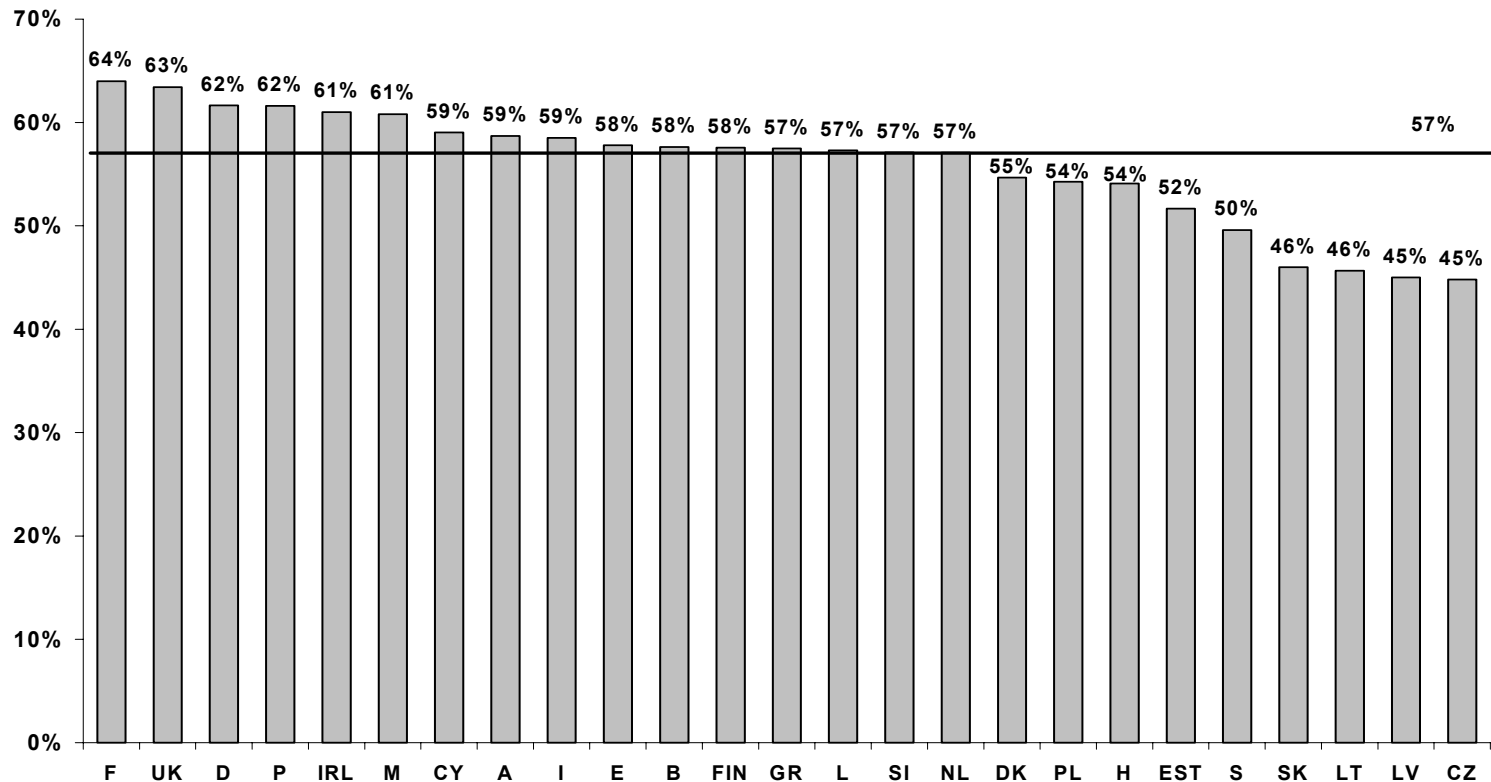
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# Excise duty rates in MS (on MPPC)

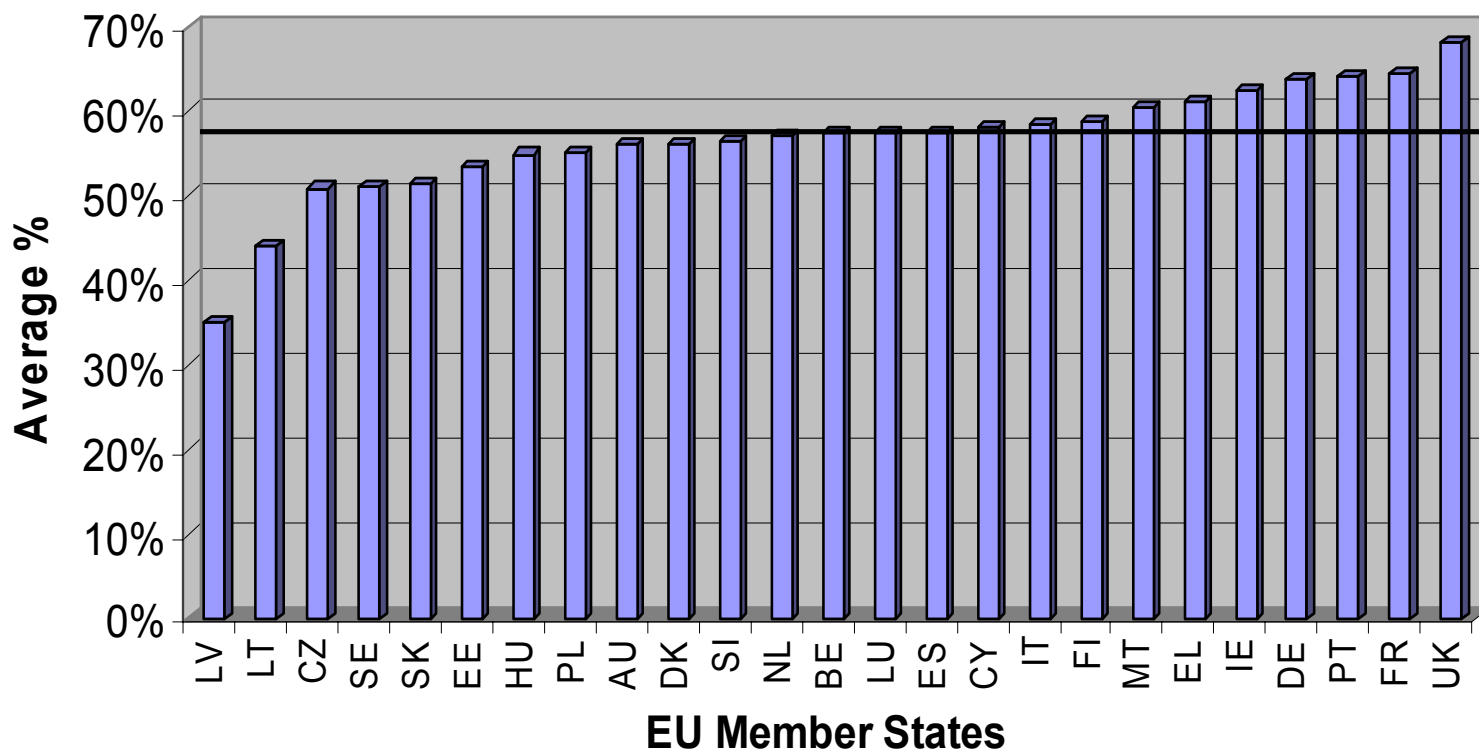
## Excise tax incidence on MPPC

Jan 2005 (% of MPPC)



# Average excise duty rates in MS

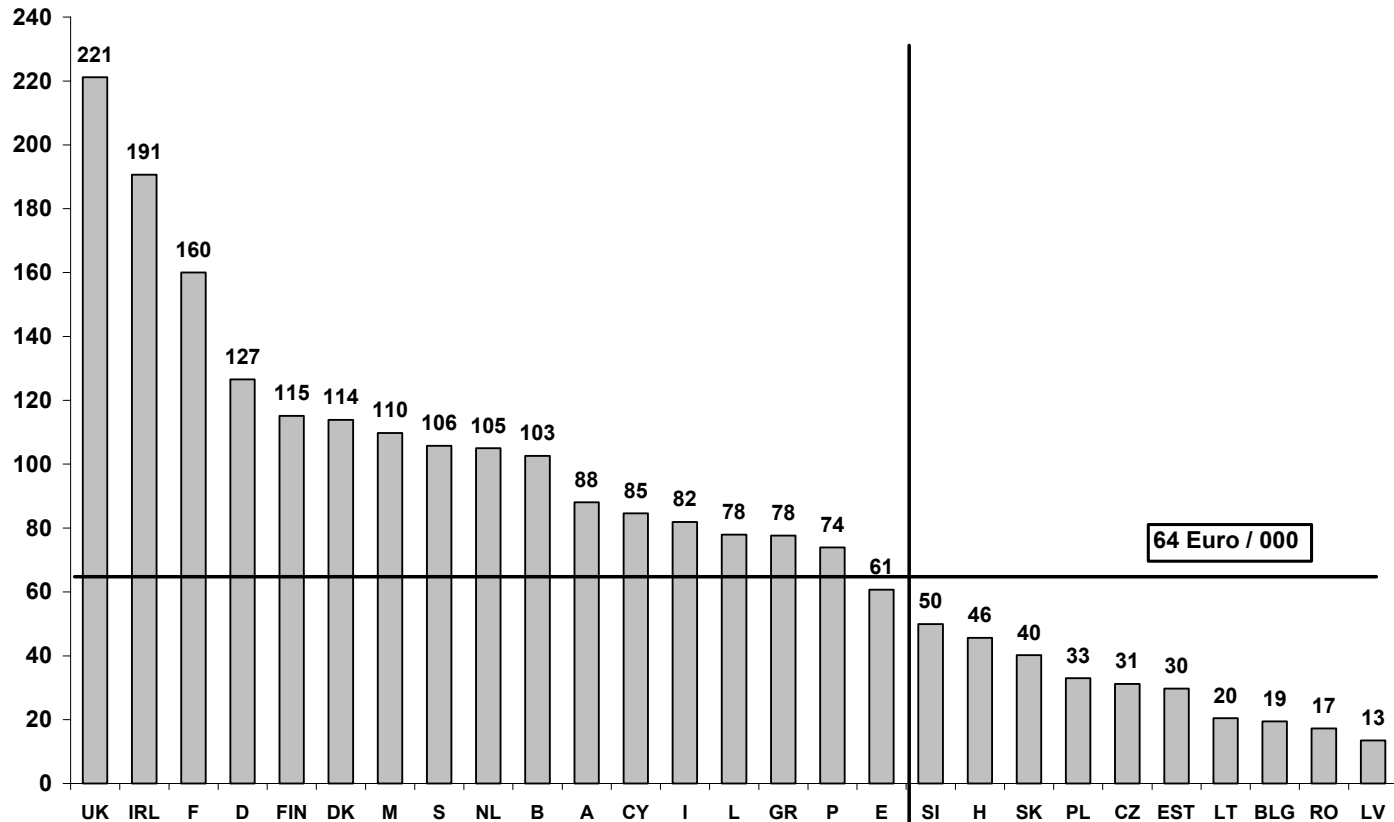
Average % of excise duties in TIRSP



# Excise duty rates in MS (in EUR/1000)

## Excise tax yield on MPPC

Jan 2005 (Euro/000)



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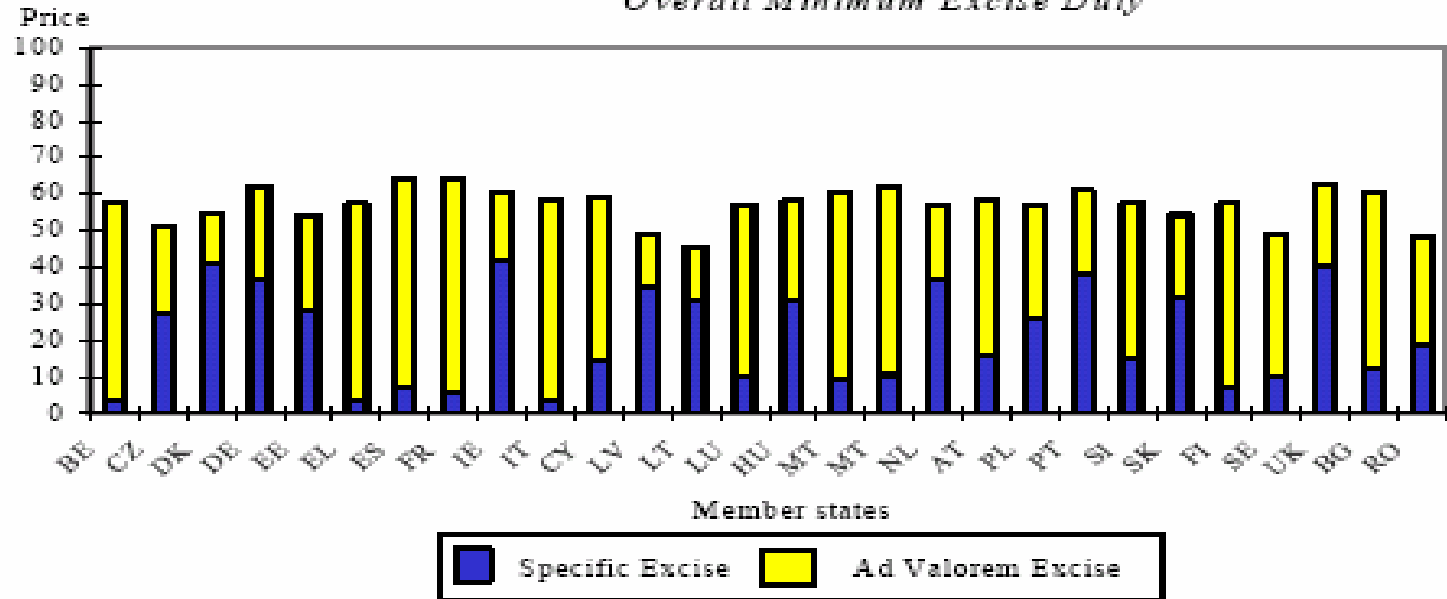


# Cigarettes

Situation as at 1 January 2006

## Overall Minimum Excise Duty

% of Retail Selling Price

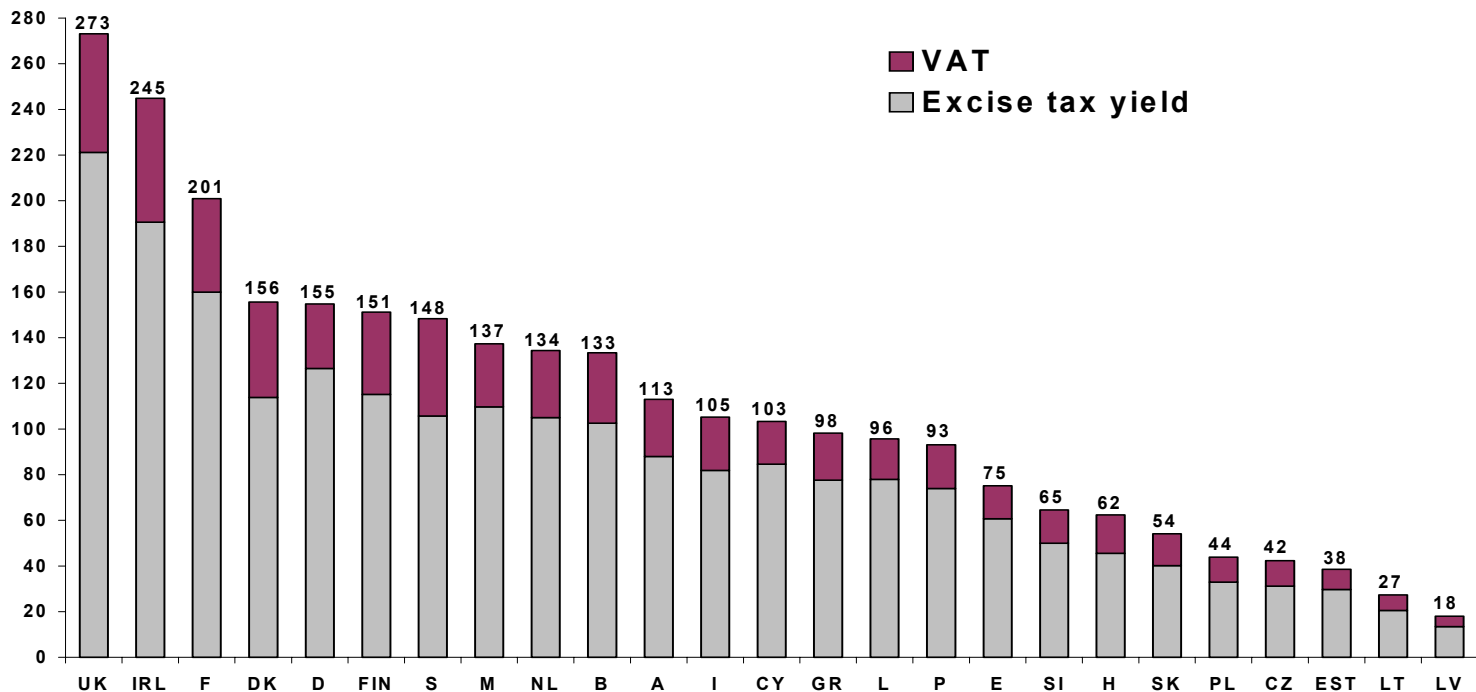


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  - Pre-tax prices (depending on purchasing power) and retail margins
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# Total tax yield (including VAT)

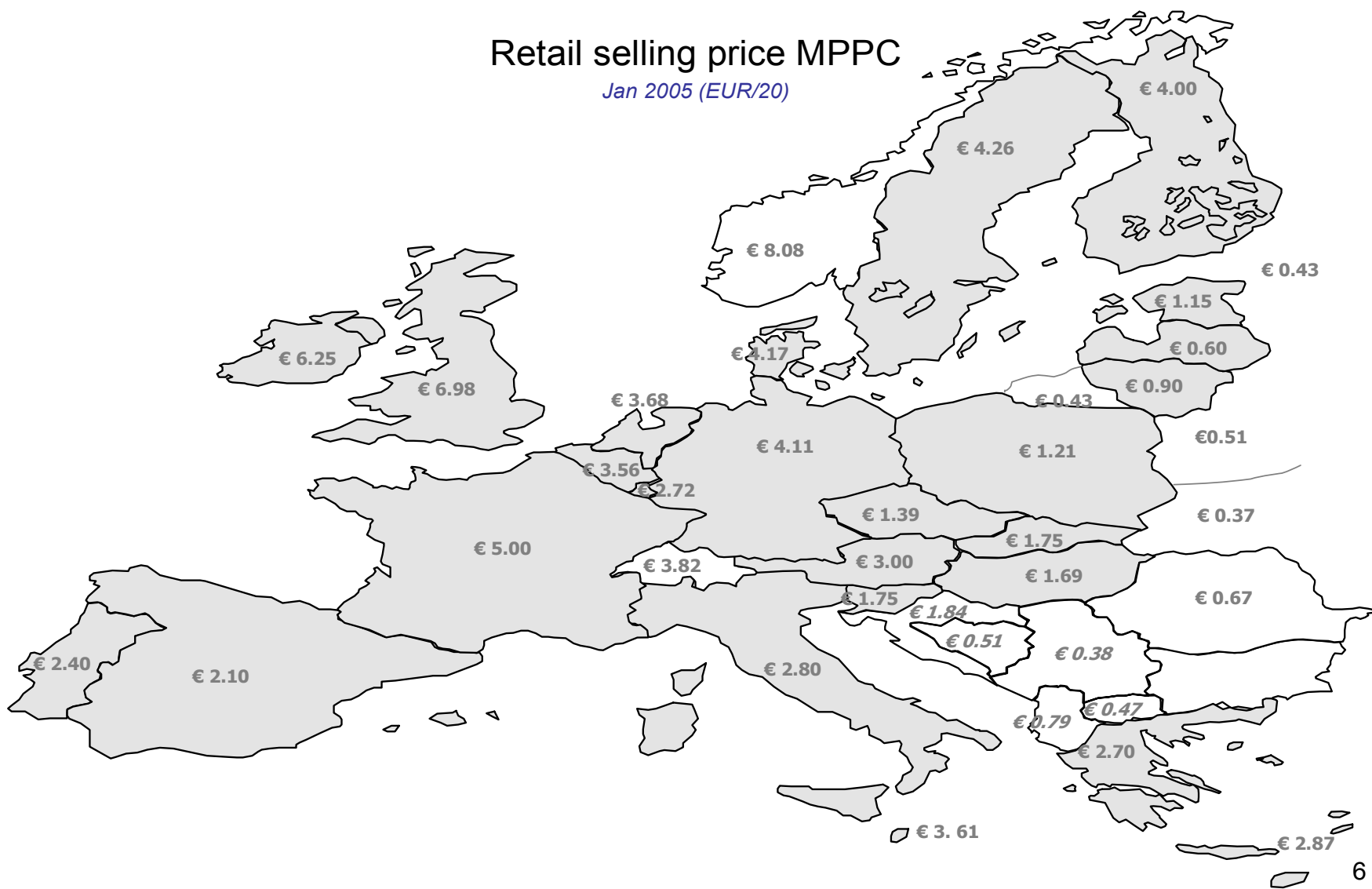
Total tax yield (excise and VAT) on MPPC  
*Jan 2005 (EUR/000)*



# TIRSP differentials in MS

Retail selling price MPPC

Jan 2005 (EUR/20)



# Tax and RSP differentials in MS (II)

- Consequences:
  - Increased cross border shopping
  - Contraband
- Countries affected:
  - France, UK, Germany (inflow from low taxing MS)
  - Low taxing MS (inflow from Romania, Russia, Belarus, Ukraine)

# Taxation of other tobacco products



# Tobacco product categories

- Cigarettes (majority of market)
- Cigars and Cigarillos
- Smoking tobacco
  - Fine-cut tobacco for the rolling of cigarettes
  - other smoking tobacco

# Minimum level of taxation

<b>Cigars and cigarillos</b>	<b>Ad valorem duty (% of max TIRSP)</b>	<b>5% of TIRSP or € 11 per 1000 items or per kg</b>
<b>Fine-cut tobacco</b>	<b>OR</b> <b>Specific duty (per kg or per number of items)</b>	<b>36% of TIRSP or € 32 per kg</b>
<b>Other smoking tobacco</b>	<b>OR</b> <b>A mixture of both</b>	<b>20% of the TIRSP or € 20 per kg</b>

# Derogation

- Transition period for France: lower excise duties can be levied to tobacco products for Corsica until 31/12/2009

# Optional minimum excise duty

- Legal basis
  - Article 3 of Directive 92/80 (other tobacco goods)
- Requirements:
  - Applied only in cases where the structure of excise duties is either ad valorem or mixed

# Recent changes and future plans

Thank you for your attention!