# EUROPEAN COMMISSION
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**UNOFFICIAL ABSTRACT OF THE**

**REPORT FROM THE COMMISSION TO THE COUNCIL**

**on Directive 2011/64/EU on the structure and rates of excise duty applied to manufactured tobacco**

## Introduction

On 8 March 2016, the Council (ECOFIN) requested the European Commission to undertake the necessary studies to submit a legislative proposal for revision of Directive 2011/64/EU of 21 July 2011 on the structure and rates of excise duty applied to manufactured tobacco … the Commission has decided to not submit a proposal for revision of Directive 2011/64/EU at this moment in time.

## Background

Directive 2011/64/EU sets out harmonised rules at EU level on the structure and rates of excise duty applied to manufactured tobacco. In particular,

a) it defines and classifies various manufactured tobacco products covered by the Directive according to their characteristics.

b) The structure of the excise duties for the different types of products is also established in this Directive.

c) The Directive was identified for evaluation under the Commission's Regulatory Fitness and Performance Programme (REFIT).

d) An external evaluation of this Directive was finalized in 2014 and was followed by a Commission Report presenting the results and conclusions of the evaluation in 2015. This report was discussed by Member States in the Council (ECOFIN) and a set of conclusions on future action in this area was adopted on 8 March 2016.

e) In order to comply with the request of the Council contained in these conclusions, the Commission started the preparation of an impact assessment and contracted an external consultant to carry out a study for this purpose. The object of the study was to contribute to the impact assessment for a possible revision of Directive 2011/64/EU. The issues analysed were among those identified in the evaluation carried out in 2014.

## Illicit trade in raw tobacco

Raw tobacco currently does not come within the scope of excisable goods as defined in Directive 2011/64/EU. During the evaluation in 2014, it was reported that raw tobacco was being diverted to the illicit circuit. This is because diverting raw tobacco to the illicit circuit could be an easier option compared to manufactured tobacco products because monitoring tools such as the Excise Movement and Control System (EMCS) are not used to monitor movements of raw tobacco. Illicit trade in raw tobacco is estimated at approximately 10 000 tonnes per year, about 1 % of the EU raw tobacco market. If cigarettes were produced from this amount of raw tobacco, this could cause a tax evasion between EUR 1 and 2 billion, amounting to 1.6 to 2.7 % of the current revenues from cigarettes.

Including raw tobacco in the scope of excisable goods would enhance control but would also impose administrative and compliance costs on all legitimate operators. These costs are high compared to the value of production; about 35 % of the market price of EU raw tobacco. Compared to the overall EU raw tobacco market, these costs would represent about 8 % of its value. This would lead to loss of competitiveness of EU-grown tobacco compared to imported tobacco. The regulatory costs consist of setting up and receiving authorisation to operate a tax warehouse and setting up and moving goods under the EMCS system. This would give an advantage to growers and first processors outside the EU which would not have to bear these costs but could still export (raw) tobacco to the EU.

Moreover, the amount of tax evaded that might possibly be recovered as a result of EMCS monitoring is unlikely to outweigh the administrative and compliance costs incurred by economic operators and, to a lesser extent, public authorities.

The Commission would therefore support the recommendation of the external study which concludes that including raw tobacco in the scope of excisable goods would be disproportionate and that similar benefits might be achievable at lower costs by a common regulatory framework for growers and first processors in the EU.

Some Member States have already introduced a national regulatory framework which requires economic operators to register and keep records of stocks and the flows of raw tobacco.

## Conclusion and way forward

In this report the Commission has explained the reasons why no proposal to revise or amend Directive 2011/64/EU will be tabled in 2017. The main reasons are the lack of data necessary to underpin a proposal for harmonized taxation of e-cigarettes and the fact that some issues identified in the evaluation of 2014 have since been solved at national level or have been settled. The question whether there is a need to propose a harmonized explicit category for e-cigarettes and Heat-not-Burn tobacco products will be re-considered in the context of the next REFIT evaluation and report on the directive due in 2019.

The REFIT evaluation will cover the outstanding issues which the external study could not conclude on including e-cigarettes and Heat-Not-Burn tobacco products. It is expected that more information will become available from, among other sources, the reporting obligation under article 20 of the Tobacco Products Directive. The Commission will therefore continue to monitor the developments related to e-cigarettes and Heat-Not-Burn tobacco products.

Finally, the Commission considers that a review of the minimum rates applicable under the Directive should also take place in parallel with the REFIT evaluation. According to Article 19, paragraph 1 of Directive 2011/64/EU the Commission is required to submit a report on the rates and structure of excise duty laid down in this Directive every four years. The last report was submitted in 2015 and the next report will be due in 2019. In the last evaluation finalized in 2014, minimum rates were not examined because some of the current transitional periods had not yet ended and not all increases had entered into force. Currently almost all Member States, except Bulgaria, Hungary and Romania, have reached the overall minimum rates. By 2019, when the next report and possible revision are due, it will have been almost 10 years since the current minimum rates were approved and no correction for the effects of inflation has been applied. In an annex to the Council Conclusions of 8 March 2016, five Member States supported the conclusion that the work on a future revision of the minimum rates should be started without delay. Moreover, bearing in mind the serious harm to health of tobacco products, it should be taken into account that article 168 of the Treaty on the functioning of the EU requires a high protection of public health and that the EU is a party to the Framework Convention on Tobacco Control (FCTC). For these reasons, the Commission now believes that the examination of the need to increase minimum rates should also take place in parallel with the REFIT evaluation. Therefore, the Commission will start the evaluation of the minimum rates in 2018.