



February 15, 2017

To: European Commission
DG TAXUD
Indirect taxes other than VAT
SPA3, 05/072
B-1049 - Brussels
Belgium

To the kind attention of
Mr. Eija HOKKANEN

To: Economisti Associati Srl
Via San Felice, 6
40122 - Bologna
Italy

To the kind attention of
Mr. Giacomo LUCHETTA

Re: public consultation on the Excise duties applied to manufactured tobacco, in the framework of the possible revision Council Directive 2011/64/EU.

Dear Sirs,

we refer to our letter of February 27, 2014, while commenting the Ramboll study recommending that suggestions to make raw tobacco excisable should be considered for further analysis (pages 71-81). The report suggested that excise could be applied at a zero-rate, and that this would assist in the fight against illegal tobacco manufacturing. We already considered, at that time, this view to be naïve and highly dangerous for the European tobacco raw tobacco sector.

Tobacco growers in the European Union produce around 180,000 tonnes of raw tobacco each year across some 100,000 hectares of farmland. The tobacco growing sector

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involves 400,000 people of which nearly 90,000 are tobacco farmers, mainly very small scale ones (less than 0,5-1 hectare).

We represent a legally compliant law abiding sector and we share with the Commission and with Member State governments the objective of eliminating the illicit trade in tobacco products. As a part of this, we fully support efforts to prevent the diversion of raw tobacco to the illegal market. However, we cannot agree that making raw tobacco excisable is an effective and proportionate solution.

Subjecting EU grown raw tobacco to excise would not prevent product being diverted to illegal manufacture, nor would it raise a single additional coin for the governments of the concerned Member States.

Tobacco grown in the European Union represents only 2.5% of world tobacco marketing and is of very high quality and integrity, has high labour and energy costs and its price on the international marketplace is high compared to analogous varieties of raw tobacco sourced from other origins (India, Brazil, Africa, etc.). The reasons that permit raw tobacco to be grown in the EU which, since crop 2009 does not receive any EU subsidy, are related to its overall integrity, sustainability and lawfulness.

The entire EU grown raw tobacco is processed by EU based first processors and the majority is sold to legitimate EU manufacturers, with a small fraction being exported in third countries to the same relevant manufacturing groups.

As such, EU tobacco growers are highly unlikely to be the source of tobacco used by illegal manufacturers. Illegal manufacturers are most likely to get almost all of their tobacco from imports. As such, for this proposal to achieve any effect, it would need to force illegal manufacturers and their overseas suppliers to declare their imports. It is completely implausible that an illegal industry would make any such declarations.

In relation to the public consultation on the Excise duties applied to manufactured tobacco, in the framework of the possible revision Council Directive 2011/64/EU, we had several interpretation problems to fill the on-line questionnaire so we decided to provide our replies concerning the areas of our interest and knowledge below, together with the explanatory information.

Without wanting to enter into details on the regulation of finished tobacco products, that are not within our area of interest, we would like to make one observation of principle regarding the section “E-cigarettes”, concerning both the so-called electronic cigarettes and the heat-not-burn products. As the representative of EU tobacco growers and first processors, it is our view that nicotine and tobacco based products with equivalent health effects should be subject to the same regulation and taxation criteria, whether or not they contain tobacco. Discriminating products based on the fact that they contain tobacco would have an adverse impact on our activities, while not addressing the objective to protect public health and representing also a violation of the principle of proportionality and equality. We would therefore hope that any regulatory intervention in this emerging market, which could be of interest for the activities of our members, be informed by an objective fact-based analysis, and not be discriminatory.



Raw tobacco (pages 24-29)

Question 1: Based on your knowledge and experience, the trade and consumption of illicit raw tobacco products are ... ?

- Growing
- Stable
- Declining

Don't know

We don't have official information on the issue and we consider also that the situation can be extremely different among the various MS. On the other side, it is not clear (also in other parts of the questionnaire) if the question refers to EU grown raw tobacco or materials imported from third countries.

Question 2: In your opinion, is there a need for additional measures at EU level to prevent and fight illicit trade and tax fraud in the field of raw tobacco?

- Yes

Maybe

- No
- Don't know

Regarding raw tobacco imported from outside the EU we simply believe that the custom controls should be intensified, but the matter is out of the scope of our members' activities.

Regarding EU grown raw tobacco we are absolutely convinced that illicit trade in the field of raw tobacco cannot be effectively combatted by excise tax legislation.

However we are equally convinced that there is merit in adopting other measures, either at EU level, or at Member State level, but within an EU homogenous legal framework, which can - and in some countries currently do - more effectively control the production, marketing and distribution of raw tobacco. Based on our experience, this is best achieved by re-introducing the mandatory requirement for tobacco growers and first processors/purchasers to be licensed and registered by the national Ministries of Agriculture and to sign cultivation contracts on a yearly crop base, supported by a contract registration system, that would be open to control, inspection and/or supervision by relevant regulatory or enforcement bodies. These cultivation contracts, registered at national level, could form an EU level transparent database.



Prior to the end of the raw tobacco CMO (until crop 2009), when the production of tobacco was still linked with the payment of direct subsidies to growers, such payments were conditioned upon the existence and registration of tobacco cultivation contracts. Such a system not only enabled the payment of subsidies to be controlled, but it also ensured that growers were incentivized to grow tobacco and only supply such raw tobacco to legitimate - i.e. recognized/licensed - first processors/purchasers.

In order to facilitate the raw tobacco traceability system we also suggest that the growers should concentrate and contract raw tobacco through Producers Organizations, as provided by Reg. (EU) 1308/2013 and not individually.

If a tobacco cultivation is found not to be under a legitimate cultivation contract after the deadline for signing the contracts, that tobacco should be confiscated and destroyed by the public authorities and law enforcement bodies.

Such a system is already in place in Italy. We note that the recent study pertaining to Bulk Tobacco¹ suggests that measures like this can be effective in reducing, to a minimum, the possible leakage of EU grown raw tobacco into the illicit market.

On the other side the same Bulk Tobacco Study enlightens the fact that Poland and Hungary, the only two EU Member States where raw tobacco is currently under some form of excise system, are countries where the issue of illicit manufacturing and marketing of raw tobacco seems not to be resolved but is even greater than in other countries scrutinized by the study.

The study also tries to demonstrate a sort of link among the overall quantity of raw tobacco grown and the illicit trade of the same in a country. This makes absolutely no sense: in Greece and Bulgaria, the first and second countries in terms of quantity produced in the area concerned, since, in those countries, almost all production is of classic oriental tobacco varieties which have a very high price and are absolutely unfit for the production of cut tobacco for RYO/MYO due to their organoleptic characteristics (these tobaccos are extremely peppery and are used only in the so called American Blend cigarettes in very small quantities).

All legitimate actors in the law-abiding tobacco supply chain² are determined to stamp out illicit trade. If a particular tobacco grower does not deliver the quantity of tobacco that he has contracted to grow and supply to a first processor/purchaser then this raises a red flag and calls to intensify the controls in the farms. This serves as a very effective

¹ Crime & Tech: Bulk Tobacco Study, 2015, www.crimetech.it/index.php?file=news&id_page=5#id18

² We acknowledge that there may always be a very small minority of rogue tobacco growers and/or other individuals who may be tempted to work outside the system disregarding whatever law or controls as may exist. They do so to criminally exploit opportunities to make profits thanks in large part to the very high levels of excise tax levied on legitimate tobacco products. In doing so, they know they are breaking the law, and will, presumably, continue to do so unless and until they are caught and convicted of a crime. To suggest that subjecting raw tobacco to excise tax would somehow stop such individuals from engaging in illicit trade is a complete nonsense. The more taxes that are imposed the greater the incentive that exists for individuals to turn to the illicit markets.

deterrent to growers otherwise tempted to engage in unlawful supply of tobacco to the illicit market. Additionally, if it were made unlawful - in all EU member states - for anyone to grow tobacco without a valid tobacco cultivation contract in place with a registered or licensed first processor/purchaser, this would serve as a vital tool for the police and other regular enforcement authorities in each member state to exercise some control in this area (with such authorities being actively supported in their efforts by the legitimate growers and processors/purchasers who have no less a vested interest in stamping out illicit trade than the fiscal authorities and tobacco product manufacturers).

Question 3: Considering the possible diversion to the illicit trade of raw tobacco and other intermediate products not covered by the Directive, please indicate how serious the following issues are, in your opinion.

	Not an issue	Minor issue	Moderate issue	Major issue	Don't know
Diversion of raw tobacco to the illicit manufacturing of tobacco products	<input type="radio"/>	<input checked="" type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Diversion of semi-processed tobacco to the illicit manufacturing of tobacco products	<input type="radio"/>	<input checked="" type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Diversion of tobacco refuse (by-products and waste) to the illicit manufacturing of tobacco products	<input checked="" type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Sale of raw and semi-processed tobacco (not duty paid) directly to consumers	<input type="radio"/>	<input checked="" type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>

Our members consider the possible diversion to the illicit trade of raw tobacco, in particular raw tobacco grown within the EU, to be an important issue that can and should be tackled but it is a relatively minor one in terms of scope and frequency when viewed in the context of the legitimate tobacco market as a whole. Therefore it seems reasonable to conclude that regulatory steps taken at local country level as well as by the tobacco industry itself are achieving some success.

In contrast with this we consider that to try to tackle the illicit trade issue by introducing excise tax controls on farmers and first processors would be equivalent to taking a sledgehammer to crack a nut and would be an inconclusive if not self-defeating futile exercise.



A system imposing excise tax on raw tobacco would be impossible to regulate let alone police in any meaningful way for various reasons, we cite the main ones but are sure that there are many more that could be mentioned.

- Scale. Whereas there are a relatively small number of EU registered tobacco product manufacturers with limited number of manufacturing facilities, there are tens of thousands of tobacco growers (each of whom would presumably need to be licensed and controlled).
- Practicality. No excise control of raw tobacco is meaningful unless the quantity (in grams or kilograms) is capable of being accounted for at each step in the process. Tobacco grows from a seed (weighing less than 0,001 gr) into a plant with a total weight which will vary, depending on variety and growing conditions, up to some kg. After harvesting and during curing, the tobacco leaves, already separated from the primary stems, will start to dry out - thus losing weight (water). During first processing the raw tobacco leaves will be subjected to threshing and re-drying procedures resulting in separation of leaf lamina from bigger veins and further changes in weight (typically 35-40% weight loss compared to the volume of loose leaves delivered by the grower).

Even after the resulting tobacco strips and tobacco refuse have been packed into separate cartons for delivery to a tobacco product manufacturer for use in their own manufacturing processes, further weight changes will still occur, which will vary depending on the conditions in which the product is stored and/or transported, while tobacco dust, grit and organic or not non tobacco related materials are destroyed as waste.

Accordingly, any system of control would need to allow for the fact that substantial changes in weight will occur. This leaves us wondering what is the point of trying to control movements of raw tobacco with reference to weight if the weight itself is subject to significant variation at all stages in the process, rendering it virtually impossible for anybody to detect with any degree of confidence whether any quantity of tobacco has disappeared into the illicit market? All this without considering that environmental damage such as flooding may occur in the farms leading to a destruction of an excised product with all the imaginable consequences.

- Common sense. It defies common sense to consider that each farmer's plot of land (also being an open space uncontrolled by any form of security) might be qualified and registered and have the proper infrastructures, as a tax warehouse and meaningfully controlled as such. The large majority of EU tobacco farms, especially in Bulgaria, Greece and Southern Italy are very small scale farms with a surface of less than half hectare.

Farmers do not have the resources that would enable them to bear the excessive administrative burdens associated with registering their premises as tax warehouses and cost of implementing and complying with EMCS and associated compliance requirements.



- Illogical. Excise tax is a consumption tax intended for application to final tobacco products to be sold at retail to final customers; raw tobacco is simply not a final tobacco product intended for final consumption but a semi-finished product.
- Counter-productive. If a farmer were to be faced with extremely costly and burdensome obligations occasioned by the imposition of excise tax on raw tobacco, without achieving any improvement for his revenue, making his activity not economically sustainable anymore, he may well decide not to register his farm under any new excise tax regulations but may decide instead either to abandon tobacco growing altogether or decide to grow tobacco, under the radar, exclusively for supply to the illicit market. In other words, the imposition of excise tax on raw tobacco might have the exact opposite effect to that which was intended and may well result in increased supplies of raw tobacco to the illicit market. On the other hand if farmers currently supplying the illicit tobacco chain exist, they will never register themselves just because an excise system have been established.
- Unfair and disproportionate treatment of EU tobacco growers and first processors. Tobacco growers and processors located outside the EU would not be subject to excise regulations imposed on growers and processors located inside the EU. This would leave EU growers and processors in a competitively much weaker position compared to their counterparts just across the border. Tobacco growing outside EU borders would then most likely flourish resulting in no reduction in the amount of tobacco supplied to the illicit market inside the EU. All that the imposition of excise tax on raw tobacco would ultimately have achieved would be to put the many thousands of legitimate EU tobacco growers and processors out of business, with no impact whatsoever on the level of illicit trade or excise tax receipts within the EU but, at the same time, giving rise to a negative impact on the economy of the EU and MS tobacco growing areas and import-export trade balance.

Question 4: Please express your agreement / disagreement with the following possible approaches to address the issue of illicit trade and tax fraud on raw tobacco and intermediate tobacco products.

	Fully disagree	Partly disagree	Neutral	Partly Agree	Agree Fully	Don't know
Regulatory revision: introducing in the Directive a specific definition and tax category for raw tobacco and relevant intermediate products, so that they are included in the excise system and covered by the control	<input checked="" type="checkbox"/>	<input type="checkbox"/>				

system (EMCS).						
Non-regulatory option: encourage the adoption of administrative approaches to the raw tobacco sector - i.e. registration of growers, processors, and tobacco transactions etc. - in line with what some Member States are already doing.	○	○	○	○	X	○
Non-regulatory option: stepping up joint efforts on monitoring and law enforcement against illicit trade of raw tobacco.	○	○	○	○	X	○

We fully disagree with the imposition of excise tax on raw tobacco or the inclusion of raw tobacco in the EMCS for the reasons outlined in our answers to earlier questions.

We support non-regulatory options, meaning non-excise tax based regulatory options as outlined in our answers to earlier questions, in particular the mandatory registration of tobacco cultivation contracts which can also be based on an EU regulation. We cannot and do not support any system of control that would impose unnecessary cost or administrative burdens on growers or processors, but we can consider supporting a system where the interests of legitimate tobacco growers and processors may be exempted from burdensome and costly bureaucracy.

The problems connected with illicit trade are not at all associated with the business operations conducted by legitimate first processors or growers. Legitimate first processors are compelled by their customers (in the main, these are large multinational tobacco product manufacturers) to ensure that raw tobacco supplied to those customers is fully traceable at each stage of the production process and are required to ensure that tobacco is grown and processed in full conformance with Good Agricultural Practices (GAP), respecting lawful, socially responsible labour practices (ALP) and ensuring that no tobacco handled by them is supplied to any party engaged in illicit trade.

If a processor fails to comply with the exacting requirements of its large cigar/cigarette manufacturing customers, that would put its entire business in jeopardy. Legitimate processors therefore have no interest or incentive to engage in illicit trade. In short, legitimate processors in the EU are professionally run, law abiding companies and subjecting them to increased regulation will therefore make absolutely no difference to the presence or absence of illicit trade in raw tobacco. Such regulation would merely add cost to their operations making the pricing of the tobacco they can offer to their customers uncompetitive compared to tobacco from non EU sources from which multinational cigarette and cigar manufacturers already source a significant quantity of the tobacco needed for their EU manufacturing operations.



In other words, the extra cost imposed on EU tobacco production could be all that it takes to render EU tobacco production unviable, putting the many thousands of farmers out of business, and leaving an even greater number of agricultural workers and employees of processors out of work and dependent on financial support (social security) from the member state in which they are located. This would lead to an increase of tobacco imports into the EU and damage the economy of the Union altogether.

Simple rules prohibiting persons, firms or companies from producing or moving raw tobacco without a tobacco cultivation contract (registered if needed with a government body in the relevant member state, much better if under an EU common legal framework) may serve as a basis on which police or other enforcement authorities can stop, search and seize tobacco and/or trucks transporting same - and take the appropriate action against any individual found in possession of raw tobacco without the necessary supporting paperwork.

Since the raw tobacco supply chain is already working in some MS with a contract registration system, it would be most logical to build any controls around that existing infrastructure, rather than implement an EU level system of excise tax controls in relation to tens of thousands of tobacco farmers and processors who completely lack the resources (administrative and financial) to cope with the complex bureaucratic and technological requirements of excise tax controls and EMCS.

Question 5: In your opinion, what is the risk of unintended adverse effects deriving from including raw tobacco and intermediate tobacco products in the scope of the Directive?

X	Low risk	Moderate risk	High risk	Don't know
The burden associated with the excise framework and the control system (EMCS) would push EU tobacco growers out of the market	<input type="radio"/>	<input type="radio"/>	<input checked="" type="radio"/>	<input type="radio"/>
The burden associated with EMCS and related obligations, would encourage more players to turn to the illicit trade	<input type="radio"/>	<input type="radio"/>	<input checked="" type="radio"/>	<input type="radio"/>
Small players would be significantly more affected than large ones, with distortive effects on competition	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input checked="" type="radio"/>
Monitoring the flows of raw tobacco and intermediate products through the excise system and the EMCS may not work for technical reasons (e.g. variation in the weight of the products through the various steps of processing)	<input type="radio"/>	<input type="radio"/>	<input checked="" type="radio"/>	<input type="radio"/>



Significant additional burden for the tax administrations	○	○	X	○
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There is a high risk of each of the adverse effects described above, for reasons we have explained in our answers to earlier questions. However, we think it is appropriate to reinforce the points raised earlier by mentioning the following.

Concerning row 3, it should be noted that the vast majority of the tens of thousands of EU tobacco farmers are “small” players, many with farms of less than 0,5-1 hectare and a consequent small annual income from tobacco production. This is in stark contrast to the resources of cigarette, cigar and other final tobacco product manufacturers, who are currently the subject to excise tax legislation and controls (including EMCS). Farmers do not possess the resources necessary to cope with the requirements of an expansion of excise tax controls/EMCS to raw tobacco.

Concerning rows 4 and 5, we have already explained the significance of the huge numbers of farmers and the variations that will occur in the weight of raw tobacco. But these are just two of the reasons why monitoring the flow of raw tobacco through the excise system will not work, and why the burden of administering raw tobacco under an excise system would be significant.

Other reasons include:

- tobacco is grown in open fields, not in buildings where access and egress is controlled using sophisticated security systems. It would be unconscionable to consider that a small tobacco farmer might be subject to considerable fiscal or other penalties, should some of his tobacco, before or after harvesting, be lost, stolen or damaged (due to fire, theft, flood or other adverse weather conditions). Any excise system would thus need to be adapted to anticipate and address these types of scenarios in an equitable manner - a virtually impossible task in our opinion.
- to exert control over tens of thousands of farmers, excise authorities would need to employ hundreds, if not thousands, of additional officers at huge and unnecessary cost to Member States. Having made such an investment, the authorities would, we expect, soon discover that this has had absolutely no impact on the level of illicit trade, considering that such trade is pursued by criminal gangs using raw tobacco grown outside the EU and smuggled into EU, and by a small number of rogue farmers or small illegal manufacturing facilities in the EU who would not, in any event, be registered, or subjected to routine controls, under any new excise system.

Not being a final tobacco product, raw tobacco/intermediate tobacco products should not be subject to excise tax (which is a tax on consumption). Accordingly, the huge additional infrastructural cost involved in expanding excise controls to raw tobacco will not raise a single additional Euro cent in excise tax revenues, so will need to be financed by other means. And, as explained in earlier answers, increased controls on legitimate



EU tobacco farmers and first processors will not decrease the incidents of illicit trade, because legitimate farmers/first processors are not involved in illicit trade today.

Question 6: Based on your knowledge and experience, how frequent are issues and disputes with the classification for tax purposes of the following products?

	Not an issue	Minor issue	Moderate issue	Major issue	Don't know
Raw and semi-processed tobacco	<input type="radio"/>				
Reconstituted tobacco (also known as 'homogenised' tobacco)	<input type="radio"/>				
Tobacco refuse (by-products and waste)	<input type="radio"/>				

It should be noted at the outset that very different considerations may apply depending upon whether tobacco is being imported into the EU, having been grown and processed outside the EU or has been grown and processed in the EU.

Based on our knowledge and experience, there have been, and continue to be, issues and disputes in relation to classification for tax purposes of raw tobacco after first processing (including tobacco refuse), but rarely, if ever, with respect to raw tobacco in its condition prior to first processing.

Such issues have occurred both in relation to:

- EU origin raw tobacco (following first processing) when being moved from a tobacco processor in one Member State to tobacco product manufacturers or other legitimate third parties located both within and outside the EU;
- raw tobacco (following first processing) grown and processed outside the EU at the point of import into the EU.

The issues have occurred on an infrequent basis, but can have very serious financial implications when they do. (For example it should be noted that a single 20 foot container containing approximately 20 tons of tobacco refuse might have a commercial value of approximately EUR 10,000. Yet, were that same container of tobacco refuse considered to be "other smoking tobacco" under Article 5 of the Directive 2011/64, it may be subject to an Excise Tax of at least EUR 2,500,000, thus more than 250 times the commercial value of the tobacco refuse).

Based on cases of which our members have knowledge, it is clear that customs and excise authorities in different Member States take different approaches in determining whether unmanufactured tobacco should be regarded as "other smoking tobacco" for excise tax purposes. Given the potentially huge financial implications for first processors and reconstituted tobacco processors, it is important that this uncertainty is removed.

This needs to be addressed by ensuring a better and consistent understanding by excise authorities across all Member States as to what should and should not be regarded as “other smoking tobacco” for excise tax purposes and, where appropriate, better defining the existing provisions of the Directive 2011/64 to bring greater clarity in this area.

Question 7: Please express your agreement / disagreement with the following possible approaches to address the issue of classification uncertainties (and related disputes), concerning raw tobacco and intermediate products.

	Fully disagree	Partly disagree	Neutral	Partly Agree	Agree Fully	Don't know
Regulatory revision: the text of Art. 5.1.(a) on smoking tobacco (see the ‘Problem Outline’ above) should be revised by specifying that ‘industrial processing’ refers to ‘industrial processing in a tax warehouse’, so as to reduce disparities in the interpretation of this provision	<input checked="" type="checkbox"/>	<input type="checkbox"/>				
Regulatory revision: the text of Art. 5.1.(b) on tobacco refuse (see the ‘Problem Outline’ above) should be revised by removing the reference to ‘retail sale’, so as to cover also bulk sale of tobacco refuse (if it can be smoked), so as to prevent subjectivity in the interpretation.	<input checked="" type="checkbox"/>	<input type="checkbox"/>				
Non-regulatory option: there is no need for a regulatory revision but - where relevant - the European Commission may provide guidance on the interpretation of the definitions used in the Directive.	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

Concerning row 1, should regulatory revision: the text of Art. 5.1.(a) on smoking tobacco (see the ‘Problem Outline’ above) be revised by specifying that ‘industrial processing’ refers to ‘industrial processing in a tax warehouse’, so as to reduce disparities in the interpretation of this provision?

We fully disagree with this for several reasons.



The suggestion to add the words “in a tax warehouse” after “industrial processing” makes no sense at all and would simply add to the existing confusion.

This is how the article would look if the change were made.

1. For the purposes of this Directive smoking tobacco shall mean:
 - a) tobacco which has been cut or otherwise split, twisted or pressed into blocks and is capable of being smoked without further industrial processing [in a tax warehouse]

At the root of any problems with interpreting Article 5 of the Directive (Smoking Tobacco), is that, unlike Article 3 (cigarettes) and Article 4 (cigars and cigarillos), Article 5 is concerned not merely with the physical content/appearance of the goods, but with the presence of one additional characteristic (which is not immediately obvious based on a visual inspection of the goods), namely, whether or not the tobacco in question is “capable of being smoked”. Of course, it is common knowledge that most things you set fire to will smoke and tobacco, not surprisingly, when in normal humidity conditions, and considering its principal use, is no exception.

We have witnessed some worrying developments, whereby excise authorities in certain Member States, have been disposed to regard raw tobacco (following first processing), that is destined for (or in the course of being delivered to) cigarette or other final tobacco product manufacturers (or even other processing industries like perfume for flavours extraction, in the case of raw tobacco refuse), to be classified as “other smoking tobacco” in its current form. This runs counter to the intent and purpose of the Directive.

The Directive clearly identifies Union manufacturers and importers as being the parties liable to excise tax and identifies a manufacturer as:

- a natural or legal person who actually prepares tobacco products and sets the maximum retail selling price for each of the Member States for which the products in question are to be released for consumption (Recital 7 of the Directive).
- a natural or legal person established in the Union who converts tobacco into manufactured products prepared for retail sale ... (Article 6 of the Directive).

Our members, being tobacco growers and first processors, as well as processors of reconstituted tobacco (which is not a finished product) are not engaged in preparing products to be released for final consumption or in setting a maximum retail price for same. It is therefore inconsistent with the terms of the Directive for excise authorities, when determining whether tobacco is “other smoking tobacco” to look only at the smoking properties of tobacco under inspection and not also at:

- the role performed by the party (e.g. raw tobacco first processor or reconstituted tobacco processors) manufacturing, transporting or importing it;
- the intended destination of the product (and the intention that it be converted by someone else into a final tobacco product intended to be released for consumption);



- The packing type for products put up for retail sale which is well defined in article 2, par. 29, 30, 31 and articles 8-11 and 14 of EU Directive 2014/40.

Our understanding is that, in order to be considered to be “other smoking tobacco” and thus subject to excise tax, the tobacco in question must fulfil the criteria in either Article 5, 1, a) or b). One criteria common to both is that the tobacco in question must be “capable of being smoked”, which, and bearing mind that excise tax is a tax on consumption, we understand to mean that a consumer must be able to purchase the tobacco in question and, without further manipulation in his part (other than rolling it in a paper or putting it in a pipe), and after lighting it, can enjoy a smoking experience that is qualitatively very similar or comparable to that of smoking fine cut tobacco, a cigarette or cigar. If it is not in such a form, then it should not be possible to conclude that the tobacco in question is capable of being smoked. And, even if the tobacco in question is capable of being smoked, no excise liability should arise in cases where it can be shown that the tobacco is a non-finished product destined for either a Union manufacturer (i.e. a party who converts tobacco into manufactured products prepared for retail sale or processes it for other uses, for instance for the extraction of perfumes or liquid nicotine) or other party outside the EU.

We encourage the EU excise authorities to support and reinforce this interpretation on a harmonized basis to ensure that unintended interpretations, adversely affecting the interests of our members, are avoided in future.

There are further problems regarding the suggestion to add the word “in a tax warehouse”. If those words were added, tobacco will be regarded as excisable goods under Art 5, 1, a), only if it is capable of being smoked without further industrial processing in a tax warehouse. So if raw tobacco is capable then of being smoked following further industrial processing conducted other than in a tax warehouse then it follows that such raw tobacco is “other smoking tobacco” and thus subject to excise tax.

For a number of reasons, the addition of such words could render all raw tobacco subject to excise tax, even tobacco still growing in a field. Here are 3 arguments:

1. to be readily capable of being smoked, tobacco needs to be cut into fine strands and this can be done using equipment that can be easily and lawfully purchased by anyone for use anywhere (i.e. not necessarily in a tax warehouse);
2. the term “tax warehouse” is probably intended to refer to EU located facilities owned by registered EU cigarette/cigar/final tobacco product manufacturers. However, EU first processors supply tobacco not only to EU located manufacturers (who own “tax warehouses”) but also to manufacturers located outside the EU (who do not, at least under the EU legal framework). Since there is no restriction on the export of raw tobacco to third countries (where it may be converted into retail products other than in a “tax warehouse”), it could be said that all raw tobacco is capable of being smoked without further industrial processing in a tax warehouse;
3. accordingly the addition of the words “in a tax warehouse” would not only fail to solve the existing problems of interpretation, it would add new uncertainties



and anomalies, potentially rendering raw tobacco, in all its forms, even when still growing in the ground, subject to excise tax.

Concerning row 2, should the text of Art. 5.1.(b) on tobacco refuse (see the ‘Problem Outline’ above) be revised by removing the reference to ‘retail sale’, so as to cover also bulk sale of tobacco refuse (if it can be smoked), so as to prevent subjectivity in the interpretation?

We fully disagree with this also. If tobacco refuse is being sold in bulk to a consumer then it might be regarded as a retail sale even under the existing wording (so the wording does not need to be altered to address sale of tobacco refuse capable of being smoked on a bulk basis to consumers). But if one were to remove the words “put up for retail sale”, one interpretation could be that tobacco refuse would be automatically subject to excise tax at point of production. This would be a ridiculous outcome that could threaten the business model of raw tobacco first processors and reconstituted tobacco processors in the EU. When raw tobacco is subjected to first processing, one of the inevitable by products is tobacco refuse (which includes, inter alia, small particles of tobacco leaves resulting from the threshing process by which leaves are separated from the large veins in the tobacco leaf). This tobacco refuse (sometimes referred to as small lamina, fines or tobacco scraps) accounts for approximately 2 to 3% of the output of tobacco first processing. Its production is unavoidable. This tobacco refuse is supplied by tobacco first processors:

- a) to manufacturers, as an intermediate product, for them to incorporate in their production of cigarettes and other final tobacco products (to which excise tax will be applied), or
- b) to reconstituted tobacco processors, who then grind said refuse into a powder, that is then combined with other ingredients to make a tobacco sheet (reconstituted tobacco), which sheet, still an intermediate product (not subject to excise tax), is then supplied to manufacturers and used as in a), or
- c) to different types of users, such as the perfume industry or producers of liquid nicotine.

As can be noted, the tobacco refuse is ultimately incorporated into a final tobacco product produced by a manufacturer (not by a grower, first processor or reconstituted tobacco processor) on which excise tax is payable.

To make tobacco refuse liable to excise tax even when not put up for retail sale, would put in jeopardy:

- i) the existing business model followed by tobacco first processors in the EU
- ii) the continued demand for EU grown tobacco. If it is no longer financially viable for law abiding EU first processors to process raw tobacco, due to the imposition of excise tax on tobacco refuse at point of production, then legitimate EU growers would need to look outside the EU for parties to purchase their loose leaf tobacco (which is just impossible to imagine due to the huge additional costs, among other reasons) or stop growing tobacco

altogether. Of course, if law abiding licensed EU tobacco processors were forced to abandon their operations, which are compulsorily located in the same growing areas mainly for cost efficiency reasons, then there is a serious risk that vastly increased quantities of raw tobacco will be supplied by growers to illicit markets (i.e. illicit markets would fill the gap resulting from the departure of lawful business).

- iii) The recycling of an industrial sub-product.

Concerning row 3, non-regulatory option: there is no need for a regulatory revision but - where relevant - the European Commission may provide guidance on the interpretation of the definitions used in the Directive.

We would agree with this but only with the provision that the guidance provided by the European Commission is consistent with that set out in earlier in this submission, making clear that neither tobacco growers and first processors going about their normal business will have their products taxed (whether capable of being smoked or not) when it is clear they are merely producing intermediate products with no intention of retailing same themselves.

Correspondence between excise and customs classification systems (pages 36-38)

Question 1: What are your views on the legal and economic issues possibly caused by the lack of a clear correspondence between the Excise Product Codes and the Combined Nomenclature codes for certain tobacco products?

	Not an issue	Minor issue	Moderate issue	Major issue	Don't know
Additional burden for competent authorities to deal with dubious and borderline cases	<input type="radio"/>				
Risk of disputes, and related burden for both competent authorities and economic operator	<input type="radio"/>				
Risk of tax losses due to the wrong classification of products	<input type="radio"/>				
'Dual coding' burden for small economic operators	<input type="radio"/>				

When EU origin tobacco is purchased and processed by Fetratob's members, no importation into the EU occurs. Accordingly, Fetratob members are not concerned with the customs classification of the tobacco they process, nor with any perceived lack of



clear correspondence, such as may well exist, between Excise Product Codes and Combined Nomenclature Codes.

However, Fetratlab members are very concerned at the inconsistent application and interpretation of existing excise tax regulations to the tobacco that they process, as is clear from the answers given to earlier questions. Those concerns need to be addressed, not with any reference to Combined Nomenclature codes, but by ensuring greater clarity exclusively in relation to the interpretation and application of excise tax regulations to “other smoking tobacco” including tobacco refuse.

Question 2: In your opinion, in which product area(s) is the lack of a clear correspondence between Excise Product Codes and Combined Nomenclature codes more problematic?

Multiple answers possible. Please tick all that apply

- Cigars/Cigarillos
- Fine-cut tobacco
- Cigarettes
- Pipe tobacco
- Water pipe tobacco
- Raw and semi-processed tobacco
- Tobacco refuse (waste)
- Expanded tobacco
- Reconstituted (homogenised) tobacco
- Don't know

Please refer to the answer we have given to the preceding Question 1.

Question 3: Please express your agreement / disagreement with the following possible approaches for a better correspondence between the excise and customs classification systems for tobacco products:

	Fully disagree	Partly disagree	Neutral	Partly Agree	Agree Fully	Don't know
Regulatory revision: The definition and categories used in the Directive 2011/64 should be harmonised with the corresponding Combined	<input type="radio"/>					

Nomenclature definitions and classifications, for the categories of products where uncertainty can be significant.						
Regulatory revision: The definition and categories used in the Directive 2011/64 should be harmonised with the corresponding Combined Nomenclature definitions and classifications, for the categories of products where uncertainty can be significant.	○	○	○	○	○	○
Non-regulatory option: There is no need for a regulatory revision but the European Commission may provide more guidance to stakeholders, e.g. through an (updated) correspondence table between Excise Product Codes and Combined Nomenclature codes.	○	○	○	○	○	○

Please refer to the answer we have given to the preceding Question 1.

Thank you very much indeed for your attention, we remain at your disposal for any need for further information or clarification.

Kindest regards.

FETRATAB
Secretary General
Carlo Sacchetto



UNITAB
Delegate Secretary
François Vedel

