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Taxation of novel tobacco products with excise duty

M A R I U S Z C H A R K I E W I C Z *

Abstract: Under EU law, certain excise goods are subject to excise duty. However, EU Member States may also levy this tax on products other than excise goods. One of such products are innovative tobacco products. These products are becoming more and more popular on the European and world market. In Poland, these products are considered excise goods. The aim of the article is to analyze and evaluate the applicable legal solutions regulating the issue of taxation with excise duty on innovative tobacco products, in the light of EU and Polish law.

Keywords: tax, excise duty, innovative tobacco products, EU law

1. INTRODUCTION

In Poland, excise duty is regulated in the Act of 6 December 2008 on excise duty,¹ according to which excise goods and passenger cars are subject to excise duty. Pursuant to Art. 2 section 1 point 1 of the aforementioned act, excise goods are energy products, electricity, alcoholic beverages, tobacco products, dried tobacco, electronic cigarette liquid and novel products specified in Annex 1 to the Excise Duty Act. Novel tobacco products are relatively new products, enjoying more and more interest on the European and global market. The aim of the article is to analyse and evaluate the applicable regulations on excise duties for this type of excise goods, in light of EU and Polish law.

2. DEFINITION AND SPECIFICITY OF NOVEL TOBACCO PRODUCTS

According to the definition provided for in Art. 2 point 14 of Directive 2014/40/EU of the European Parliament and of the Council of 3 April 2014 on the approximation of the statutory, executive and administrative regulations of the Member States on the manufacture, presentation and sale of tobacco products and related products and repealing Directive 2001/37/EC,² “novel tobacco product” means a tobacco product that is not a cigarette, roll-your-own tobacco, pipe tobacco, waterpipe tobacco, cigar, cigarillo, chewing tobacco, nasal or oral tobacco, which is placed on the market after 19 May 2014. However, in light of Art. 2 section 1 point 36 of the EDA, novel products are products which are: a) a mixture containing tobacco or dried tobacco, b) a mixture referred to in point (a), a, and containing a separate liquid for electronic cigarettes – other than the products referred to in Article 1. 98 sec. 1 and Art. 99a sec. 1, which deliver the aerosol without burning the mixture.

It follows from the above regulation that novel products are products that are a mixture containing tobacco or dried tobacco, as well as products consisting of both a mixture containing tobacco or dried tobacco, and containing a separate liquid for electronic cigarettes, which deliver an aerosol without burning the mixture. Therefore, novel products are products other than cigarettes, smoking tobacco, cigars, cigarillos or dried tobacco, in which no combustion process takes place. At

the same time, it should be emphasised that the above definition does not include devices used to heat these mixtures.³ These devices are necessary for the use of this type of product. In the case of novel products, the combustion process does not take place, and the cartridge in the form of a specially prepared mixture is heated in an electronic device designed for this purpose; as a result, no smoke is emitted, but an aerosol instead.

Manufacturers of heated tobacco indicate that the aerosol produced when the mixture is heated contains much fewer harmful substances than cigarette smoke. This is also confirmed by research conducted by various institutions specialising in research on the harmfulness of tobacco products. Among other things, the authorisation decisions issued by the US Food and Drug Administration (FDA) in favour of the IQOS tobacco heating device indicated that the IQOS tobacco heating system,⁴ which does not burn tobacco, only heats it, significantly reduces the production of harmful chemicals compared to cigarette smoke. In addition, IQOS aerosols contain significantly lower levels of potential carcinogens and toxic chemicals that can damage the respiratory or reproductive systems.

3. HARMONISATION OF EXCISE DUTY ON NOVEL TOBACCO PRODUCTS

Excise duty is subject to harmonisation under EU law. Tax harmonisation is a process as a result of which the tax systems of various Member States are subject to unification so that tax issues do not affect the flow of goods, services and factors of production between these countries.⁵ The basic legal act regulating excise duty taxation in the territory of the European Union is Council Directive 2008/118/EC of 16 December 2008 concerning the general arrangements for excise duty and repealing Directive 92/12/EEC.⁶

However, the EU legislator did not decide to introduce uniform rules of taxation for novel tobacco

products with an excise duty. It should be pointed out here that novel products, like electronic cigarettes and liquids for electronic cigarettes, are not subject to harmonised excise duty at the EU level with regard to the structure and rates of excise duty, as well as the production and movement of excise goods.⁷ These products are not subject to the harmonisation of taxation with excise duty pursuant to Council Directive 2008/118/EC, so EU Member States are not obliged to tax novel products with excise duty.⁸ Novel products are not considered tobacco products within the meaning of the aforementioned directive. Likewise, Council Directive 2011/64/EU of 21 June 2011 on the structure and rates of excise duty applied to manufactured tobacco⁹ does not regard these products as tobacco products.

The issue of taxing novel tobacco products with excise duty was also not addressed in Council Directive (EU) 2020/262 of 19 December 2019 laying down the general arrangements for excise duty (recast),¹⁰ which will apply to excise duty in the territory of the European Union from 13 February 2023 (Directive 2008/118/EC will expire on that date). Article 1 section 1 point c of Directive 2020/262 recognises as excise goods only tobacco products within the meaning of Directive 2011/64/EU, which, as already indicated, does not recognise novel tobacco products as tobacco products.

Nevertheless, it should be noted that work is currently underway in the European Union to amend the excise duty directive in the field of novel products as well. In the information sent by the Chancellery of the Prime Minister to the Sejm and the Senate of the Republic of Poland on the participation of the Republic of Poland in the work of the European Union in January-June 2020 in the field of excise duty, it was indicated that the Council's work in the period in question focused on the transformation of the tobacco directive 2011/64/EU on the structure and rates of excise duty applied to manufactured tobacco, and consultations continued with Member States on the draft amendment to the Alcohol Directive 92/83/EEC on the harmonisation of the structure of excise duties on alcohol and alcoholic beverages. The Croatian

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Presidency presented draft conclusions regarding Council Directive 2011/64/EU in response to the Evaluation Report, which were agreed and then adopted as a document on 2 June 2020.¹¹

In its conclusions, the Council points out that changes to Directive 2011/64/EU are necessary for the proper functioning of the internal market and to ensure a high level of health protection across the EU. In the Council's assessment, the current provisions of Directive 2011/64/EU have become less effective because their scope is no longer sufficient or too narrow to meet current and future challenges for certain products such as e-cigarette nicotine liquids, heated tobacco products and other types of next-generation tobacco products that enter the market. Therefore, there is an urgent need to modernise the EU regulatory framework to meet the current and future challenges of the functioning of the internal market by harmonising the definition and taxation of novel products, including tobacco-substitute products, whether they contain nicotine or not – in order to avoid legal uncertainty and regulatory differences in the EU, take relevant good practices and experience gained by Member States in this field into account, and Directive 2011/64/EU, including the objective of defining different types of tobacco product with different characteristics and their method of use.¹²

4. STRUCTURE OF TAXATION OF NOVEL TOBACCO PRODUCTS WITH EXCISE DUTY IN POLAND

Currently, an increasing number of European Union Member States tax novel products with excise duty (e.g. Italy, Romania, Slovenia, Latvia, Hungary, France and Great Britain). In Poland, taxation with excise duty on novel products was introduced under the Act of 12 December 2017 amending the Excise Duty Act,¹³ which entered into force on 1 February 2018. General provisions on the taxation of excise goods with excise duty apply to novel products, including those relating to the subject

of taxation, the emergence of a tax obligation, taxation of shortages, properties of tax authorities, registration of entities, tax declarations and excise duty payment deadlines.

The basis for taxing novel products is their quantity expressed in kilograms (Article 99c section 3 of the EDA). It should be noted here that adopting the weight of the tobacco mixture contained in the product as the tax base for excise duty is a justified and rational solution. Novel products can appear in various forms, ranging from a roll of tobacco, through loose tobacco to be placed in a heating device, to hybrid products, where, apart from the heated tobacco, there is also a liquid with nicotine or producing a characteristic flavour. The adoption of the weight of the mixture as the tax base also significantly facilitates its calculation and collection.

The excise duty rate on novel products amounts to PLN 155.79 for each kilogram and 32.05% of the weighted average retail selling price of smoking tobacco (Article 99c section 4 of the EDA). For the purposes of determining the excise duty rate on novel products, the weighted average retail selling price of smoking tobacco is used, calculated based on data for the first 10 months of the year preceding the calendar year for which the weighted average retail selling price of smoking tobacco is calculated (Article 99c section 6 of the EDA). In the justification to the draft of the aforementioned act, it was indicated that the excise duty rate for novel products was set at the same level as for smoking tobacco, due to the fact that novel products contain tobacco and consumers use them to deliver nicotine to the body. The only difference is that for the novel products, the weighted average retail selling price of smoking tobacco was used directly as one of the ingredients, and not the maximum retail price, as is the case for smoking tobacco. This is aimed at avoiding the obligation of producers to print the maximum retail price on the unit packaging, because the novel products are characterised by a great variety of technical solutions and shapes, which in some cases could make it impossible to print such a maximum price on the packaging. Moreover, such a legislative solution will make it possible to

automatically adjust the rate for novel products to market realities, as the weighted average retail selling price of smoking tobacco is determined annually on the basis of market data from the year preceding the calendar year, and published by way of an announcement.¹⁴

It is worth emphasising here that most European countries have decided to tax novel products with a lower excise duty rate than traditional cigarettes. The same applies in Poland. The basic rate of excise duty on cigarettes is PLN 228.10 for 1000 pieces, and 32.05% of the maximum retail price, with the minimum excise duty on cigarettes being 100% of the total amount of excise duty calculated on the price equal to the weighted average retail selling price of cigarettes (Art. 99 sections 2 and 4 of the EDA). This distinction seems to be fully justified, since numerous scientific studies indicate that the novel products are potentially less harmful to health. Undoubtedly, tax policy and the level of taxation should take this circumstance into account. One of the main goals of imposing excise duty is to increase the tax burden on those areas of activity that society wants to limit. Taxation with excise duty is designed to reduce the demand for products se-

lected by the state that have a harmful effect on human health (e.g. tobacco products or alcoholic beverages) or pollute the environment (e.g. petroleum products).^{15t}

5. CONCLUSIONS

As mentioned above, work is currently underway within the European Union to amend the scope of the directive regulating the general principles of excise taxation. One of the objectives of the planned amendment is to make novel tobacco products subject to excise duty tax by EU Member States. At the same time, the need in this respect to harmonise the definition and method of taxation for this type of excise goods is emphasised, which should be carried out taking good practices and experience gained so far by the Member States into account. It should also be noted that when establishing the principles for taxing novel tobacco products, one should not only define this type of goods as an excise category separate from tobacco products, based on the attribute of not burning tobacco, but also – due to the lower harm to health – set the rate of excise duty on these products at a level significantly lower than that of traditional tobacco products (cigarettes).

Notes

- 1 Journal Of Laws of 2020, item 722; hereinafter referred to as EDA (Excise Duty Act)
- 2 Journal of Laws EU.L.2014.127.1.
- 3 Individual tax ruling of the Director of National Treasury Information of April 8, 2020, No. 0111-KDIB3-3.4013.11.2020.2.JS, <http://sip.mf.gov.pl>.
- 4 FDA permits sale of IQOS Tobacco Heating System through premarket tobacco product application pathway; <https://www.fda.gov/news-events/press-announcements/fda-permits-sale-iqos-tobacco-heating-system-through-premarket-tobacco-product-application-pathway>
- 5 FDA Authorizes Marketing of IQOS Tobacco Heating System with 'Reduced Exposure' Information; <https://www.fda.gov/news-events/press-announcements/fda-authorizes-marketing-iqos-tobacco-heating-system-reduced-exposure-information>
- 6 M. Piłatowski, *Harmonisation of taxes in the EU in the era of economic changes*, Scientific Journal of the University of Szczecin 2012, No. 52.
- 7 Journal of Laws EU.L.2009.9.12.
- 8 The justification for the government's bill amending the Excise Duty Act, Sejm paper No. 1963, www.sejm.gov.pl.
- 9 Statement by K. Lasiński-Sulecki Ph.D. for eNewsroom; <https://www.youtube.com/watch?v=xX0wN0H4eSo>
- 10 Journal of Laws EU.L..2011.176.24.
- 11 Journal of Laws EU.L.2020.58.4.
- 12 Information for the Sejm and Senate of the Republic of Poland on the participation of the Republic of Poland in the work of the European Union in January-June 2020; www.senat.gov.pl.

12 Draft Council conclusions on the structure and rates of excise duty applied to manufactured tobacco of 20 May 2020, <https://data.consilium.europa.eu/doc/document/ST-8093-2020-INIT/pl/pdf>.

13 Journal of Laws. from 2018, item 137.

14 Justification for the government bill amending the Excise Duty Act, Sejm paper No. 1963, www.sejm.gov.pl.

15 R. Rosiński, Fiscal aspects of excise duty in the European Union countries, *Scientific Journal of the University of Szczecin* 2015, No. 76.