



WORKING GROUPS



TOBACCO PRODUCTS WORKING GROUP



CHAIRMAN:

VASILI GRUZDEV,
JTI RUSSIA

The AEB Tobacco Products Working Group was created in 2013. It unites manufacturers of tobacco and nicotine goods, the joint market share of which amounts to about 95%¹, and total investments in the Russian economy of which have exceeded USD 8 billion.

The Working Group aims to ensure the generation of a sustainable and predictable legislative and taxation regime in the sector, advocating clear regulatory norms in the regulation of the production and circulation of tobacco goods, adoption of measures for the prevention of their illegal trade,

and also the reasonable regulation of the production and circulation of innovative nicotine products.

THE SYSTEM OF EXCISE TAXATION ON TOBACCO AND NICOTINE GOODS BASED ON A THREE-YEAR PLANNING CYCLE IN THE TAX CODE

The approach to the three-year planning of excise taxation in the Russian tobacco industry, established in the current tax legislation, conforms to the leading international practices in the sphere of tax policy.

¹ According to the Nielsen audit of Q3 2021 retail data

The last decade has been characterised by a growth of the tax burden and decrease in the affordability of legal tobacco products. As a result of the long-term growth of excise taxes and the decreasing affordability of legal cigarettes, the Russian market is saturated with illegal products, and the legal market is shrinking due to a material difference in excise rates for tobacco products between EAEU states (a difference in excise rates between cigarettes and other nicotine products in the EAEU and Russia results in an end difference in final consumer prices by a factor of 2 or 3). As the result, losses of budget income from excises and VAT, as experts assess, amounted to more than RUB 100 billion in 2021. The missing budgetary income, resulting from the growth of the tax burden on the sector and preservation of the extant high share of illegal products on the Russian tobacco market, will continue growing.

While before 2017 the state's fiscal policy of increasing excise rates for tobacco products had caused a certain increase in proceeds to the federal budget and a lowered share for the illegal cigarette trade, in the past 3 years, despite the continuing growth of excise rates, state budgetary income has been dropping due to the contraction of the legal market. Since 2021, a severe (20%) increase in excise rates for tobacco and nicotine products and the growth of the ad valorem component to 16% has taken place, which has caused a significant increase in the average price per pack of cigarettes in Russia in 2021, to RUB 140. Against the background of the stagnation of the real disposable income of the population and with illegal cigarettes available on the market at RUB 50-70 per pack, a portion of consumers is switching to illegal products.

A rational approach to the indexation of excise rates for tobacco and nicotine products would involve a predictable and gradual increase of the rates, proportional to the inflation rate, as estimated by the Russian Government, the real disposable income of consumers, and the parameters of the Agreement on the Principles of Introduction of Tax Policies in the Area of Excise Rates for Tobacco Products of the Member States of EAEU.

RECOMMENDATIONS

- It is recommended to continue the existing effective policy on the excise taxation of tobacco and nicotine goods based on the three-year planning cycle, in future avoiding the increase of tax rates in the already approved three-year period by a value exceeding the inflation rate, and with regard to the need for further harmonization of taxation on tobacco and nicotine products in EAEU countries. Assurance of moderate excise rate growth in order to avoid an increase in illegal trade could provide for an increase of tax proceeds and a gradual decrease in the consumption of tobacco goods.

ILLEGAL TRADE IN TOBACCO GOODS AND NICOTINE PRODUCTS

According to Nielsen Analytical Agency, in Q3 2019, the share of illegal tobacco products in the Russian Federation reached the maximum value – 15.6% of the total market volume. In Q3 2020, against the background of the anti-pandemic restrictions, the share of illegal tobacco products on the Russian market dropped to 7%. With the gradual normalization of the COVID-19 situation in the country, removal of the restrictions, and given the material increase in excise rates on tobacco products from January 1, 2021, in Q1 2021 it reach 10.7% and in Q2 it increased to 12.8%. Over 50% of illegal tobacco products arrive in Russia from EAEU member states. The smallest share is attributed to products from the Republic of Belarus – 42% in Q2 2021, as explained by an equivalent differentiation of excise rates between Russia and Belarus and the resulting difference in consumer prices for tobacco products.

Even though over the past few years the executive and legislative bodies of the Russian Federation have adopted a number of steps aimed at preventing the illegal circulation of tobacco products on the domestic market, the existing set of measures and tools, including the expanded digital labeling system, cannot stem the flow of illegal products arriving to Russia primarily from EAEU countries, resulting in the need for the adoption of additional legislative amendments and a systemic approach to their execution.

The working practice of the tobacco sector after a full-scale implementation of the labeling and traceability system from June 1, 2020 confirmed its effectiveness in keeping illegal tobacco products from penetrating legal trade channels. At the same time, the import of illegal products from adjacent countries continues in the form of sales that contravene the requirements on the use of online cash offices and the state information system for goods labeling (SIS GL). In 2021, the inflow of imports of single-use vapes which, due to a lack of technical regulations and mandatory labeling and, as a result of exceeding the permissible maximum nicotine concentration, has become a significant factor in involving the underage in nicotine consumption, has grown materially.

RECOMMENDATIONS

- It is necessary to develop and adopt a set of measures aimed at ensuring the transparency of the process of transit, export and cross-border movement of tobacco products from the Union member states through Russia, which would guarantee either the removal of the transit tobacco products from Russia or excise payments at the current Russian rates.
- To prevent the illegal imports of excisable products from EAEU member states, it would be advisable to accelerate the introduction in Russia of criminal liability for the large-scale illegal movement of alcohol, tobacco, and nicotine



- products across the state border of the Russian Federation with EAEU member states. The implementation of this proposal is provided for in the action plan for implementing the Strategy for Preventing the Illegal Circulation of Industrial Products in the Russian Federation until 2025 as it includes alcohol, tobacco, and nicotine goods in the list of strategically important products and resources for the purposes of Article 226 of the Criminal Code of the Russian Federation, and also of important goods and resources, for which a value in excess of RUB 100,000 is considered a large amount.
- › In order to reduce the expenses incurred by the state in connection with the need for lengthy storage of tobacco products and the means of their manufacture and the removal thereof from illegal circulation, it is necessary in part to specify the provisions of the Code of Criminal Procedure of Russia that determine the procedure for the removal from circulation and mandatory destruction of equipment for the manufacture of tobacco products, stock, raw materials and the means of their illegal production. At the same time, it is necessary to make revisions to the Russian Criminal Code by establishing criminal liability

for the large-scale and major production and circulation of tobacco products, unmarked with identification means (digital labeling) or marked with deliberately false means of identification.

- › It is necessary to expand the list of products subject to mandatory labeling, including all types of nicotine products, particularly to ensure a smooth transition from the experiment to the mandatory labeling and tracing of sticks for heated tobacco systems, to adopt the Resolution of the Russian Government on carrying out an experiment for labeling nicotine-containing liquids and electronic means of delivery of nicotine-containing liquids, and for completion of the experiment, accelerating the transition to their mandatory labeling and tracing.



**More information on the
Committee page**