

## **Philip Morris Limited submission to HM Treasury for Budget 2017/18**

### **1. Summary**

Philip Morris International (“PMI”) is the world’s leading international tobacco company. Philip Morris Limited (“PML”) is the UK & Ireland subsidiary of PMI.

Cigarette smoking causes serious disease and is addictive. The best way to avoid the harms of smoking is never to start, or to quit. Excise has played and can still play an important role in addressing the issue, as part of a broader fiscal and health policy. For this reason, we welcome the decision of the Government in the 2016/17 Budget to implement a Minimum Excise Tax (“MET”) on cigarettes.

While there is no substitute for quitting, we believe that harm reduction (i.e., promoting safer alternatives to those who would otherwise still smoke cigarettes), can bring significant public health benefits. This is important because there are still approximately 1 billion smokers globally, including approximately 9 million in the UK.<sup>1</sup>

We view harm reduction as an essential element of public health policy, and fully endorse regulatory and fiscal policies that enable and promote fast consumer switching from combustible tobacco products to reduced risk alternatives, including e-cigarettes, heated tobacco products and other non-combustible nicotine and tobacco products.

Our priority is clear – to switch, as quickly as possible, hundreds of millions of adult smokers across the world to less harmful alternatives than continued smoking.

### **2. Technology makes a ‘smoke-free’ UK achievable sooner**

Technological innovation is transforming our industry with the emergence of a wide range of non-combustible (‘smoke-free’) nicotine products that deliver nicotine with lower levels of harmful constituents than in cigarette smoke. This has led a range of businesses, from the established tobacco industry, to entrepreneurial start-ups, on a path of constant innovation.

Adult smokers are clearly interested in exploring alternative ways to consume nicotine that are lower risk than smoking cigarettes. The rapid rise of e-cigarettes, which approximately 80% of UK adult smokers have tried, demonstrates this, and the potential for harm reduction.<sup>2</sup> A report from ASH estimated that there were 2.8m e-cigarette users in the UK in 2016, almost all of whom were smokers (dual using cigarettes and e-cigarettes) or ex-smokers who had quit.<sup>3</sup> This represented an increase of 400% in four years,<sup>4</sup> making the UK the second largest e-cigarette market after the US. Almost half (1.3m) of these e-cigarette users no longer smoke any combustible tobacco.<sup>5</sup>

Although e-cigarettes have helped over a million UK smokers quit, the same ASH study found that the majority of UK smokers who had tried e-cigarettes went back to smoking combustible tobacco.<sup>6</sup> This

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<sup>1</sup> See <http://www.who.int/mediacentre/factsheets/fs339/en/> and ASH ‘Smoking Statistics’, June 2016.

<sup>2</sup> See ASH factsheet, “Use of electronic cigarettes (vapourisers) among adults in Great Britain”, May 2016 at Figure 2.

<sup>3</sup> See *ibid* at page 2.

<sup>4</sup> See *ibid* at page 2.

<sup>5</sup> See *ibid* at page 2.

<sup>6</sup> See *ibid* at Figure 2.

implies that while many want a safer alternative to cigarettes, they have not yet found one that helps them switch completely.

We believe that no single alternative will enable all adult smokers to switch completely. We are therefore investing in researching, developing and commercialising a range of Reduced Risk Products (“RRPs”).<sup>7</sup> PML currently sells two types in the UK.

- In 2014, we entered the e-cigarette market, through the acquisition of Nicocigs Ltd., a leading supplier of e-cigarettes in the UK and Ireland, and owner of the ‘Nicocigs’ and ‘Vivid’ brands. Through Nicocigs we also recently tested in Birmingham an innovative new e-cigarette technology, ‘MESH’.
- In November 2016, we commercialised a non-combustible tobacco product, the Electrically Heated Tobacco Product (branded ‘Heets’ in the UK), together with an electric device under the brand name IQOS. By heating rather than burning tobacco, IQOS/Heets generate a nicotine containing vapour that yields on average less than 10% of the levels of harmful constituents found in cigarette smoke.<sup>8</sup>

### **3. How the Government can use tax policy to help deliver a smoke-free UK**

Our objective is to convince all adult smokers that intend to continue smoking to switch to RRP as soon as possible. Realising this ‘smoke-free’ future will require supportive government policy to incentivise behavioural change. Taxation is an important tool to encourage switching among those not inclined to quit. It will also need to be closely co-ordinated with regulatory policy.

It is our view that, ultimately, nicotine and tobacco products should be taxed according to their risk profile (i.e.: higher risk-higher tax, lower risk-lower tax) linked to a regulatory framework that would include the standards for assessing risk reduction. The first step has already been taken in the case of e-cigarettes, which were assessed by Public Health England and the Royal College of Physicians as around 95% less harmful than smoking cigarettes.<sup>9</sup> This finding informs the policy of not applying excise duty to these products.

We urge the Government to commission its own independent scientific assessment of the relative risks of non-combustible alternatives to cigarettes, including novel smokeless tobacco products. If/when such products are assessed as being lower risk compared to combustible tobacco products, the Government should consider reforming the excise system. This would imply significantly lower or zero excise duties on non-combustible compared to combustible tobacco products.

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<sup>7</sup> Reduced-Risk Products (“RRPs”) is the term we use to refer to products that present, are likely to present, or have the potential to present less risk of harm to smokers who switch to these products versus continued smoking. We have a range of RRP in various stages of development, scientific assessment and commercialization. Because our RRP do not burn tobacco, they produce far lower quantities of harmful and potentially harmful compounds than found in cigarette smoke.

<sup>8</sup> Average of the reductions in the concentrations (weight per stick) of individual harmful and potentially harmful constituents measured in the IQOS™ aerosol compared to the smoke from a standard 9.4 mg ‘tar’ reference cigarette (3R4F). Aerosol and smoke collections performed under the Health Canada Intense machine-smoking regime (55 mL puff volume, 2 second puff duration, 30 second interval puff). Reduction calculations exclude nicotine, glycerine and water.

<sup>9</sup> <https://www.gov.uk/government/news/e-cigarettes-around-95-less-harmful-than-tobacco-estimates-landmark-review> and <https://www.rcplondon.ac.uk/projects/outputs/nicotine-without-smoke-tobacco-harm-reduction-0>

Adult smokers would have a compelling incentive to switch from combustible tobacco if non-combustible alternatives were both independently proven to be reduced risk, and attracted a lower rate of tax, making them cheaper. This could be achieved by imposing greater excise duty on combustible tobacco, a higher MET for cigarettes, and applying a separate lower excise regime to products found to present lower risk.

#### **4. PMI's views on the Budget 2017/18**

We recognise the role that excise tax can play in reducing demand for combustible tobacco products, as part of a holistic regulatory approach that, among other things, seeks to mitigate the risks of illicit trade. We support proportionate tax increases, as long as the risk for illicit trade is factored in and they are part of a broader fiscal and public health policy that incentivises switching to reduced risk alternatives. We would encourage the Government to consider how it can use all available policy levers, not just tax, to incentivise switching away from combustible tobacco (for those not quitting completely).

The Government announced in the 2016/17 Budget that it would introduce an MET on cigarettes in the Finance Bill 2017. The draft Finance Bill did not indicate the level at which the MET would take effect. We support the MET in principle, as long as it is not used to push up prices excessively (although our view remains that a higher specific ratio in exchange for lower ad valorem duty would be a simpler and more effective approach). We believe the MET should be set around the level of the excise duty borne by the most popular price in the market (adjusted pro rata to take account of the new requirement for larger minimum pack sizes), and subsequently adjusted regularly in line with excise increases.

#### **5. Minimising the threat of illicit trade**

According to HMRC, 13% of cigarettes were illegal in 2015/16, compared to 7% in 2014/15, costing the taxpayer £2.4bn.<sup>10</sup> The Government should consider the magnitude of any excise increase carefully. While steady increases in taxation can be more easily sustained, sudden, sharper increments run the risk of encouraging switching to cheaper black market combustible tobacco. This results in losses for both the Exchequer and public health.

The UK has earned global recognition for its success in fighting illicit tobacco, and we welcome the Government's continuing commitment in this area, including additional investment in Border Force, and HMRC's newly published consultation on sanctions for illicit trade offences. Additional revenue neutral policies we would support include rapid ratification of the World Health Organisation's Framework Convention on Tobacco Control Protocol to Eliminate Trade in Illicit Tobacco Products, a register of tobacco retailers in England (to mirror the successful Scottish model), and agreement on how to regulate the tracking and tracing of tobacco products through the supply chain. With respect to the latter, we would urge the Government to support regulation and technology that embrace open standards, as this stimulates competition, leading to more effective solutions at lower prices when compared to monopolistic providers.

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<sup>10</sup> [https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/561322/HMRC-tobacco-tax-gap-estimates-2016.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/561322/HMRC-tobacco-tax-gap-estimates-2016.pdf)

## **6. Conclusion**

PML calls on the Government to:

1. Commission research to validate independently the risk profile of novel non-combustible products, such as heated tobacco products, relative to the risk profile of cigarettes.
2. Continue to invest in anti-illicit trade measures, and adopt the revenue neutral policies above.
3. Introduce a Minimum Excise Tax but at a rate that does not risk increasing levels of illicit trade.
4. Increase tobacco taxation gradually at a proportionate rate to hasten switching to less harmful alternatives.
5. If the Government concludes that a product presents less risk of harm than cigarette smoking, take measures to encourage smokers to switch. This should include differential tax treatment.