

NOTE OF MEETING – JAPAN TOBACCO INTERNATIONAL (JTI) AND DH

Impact Assessment (IA) for Standardised Packaging of Tobacco Products

Wellington House
Tuesday 5th February 2013

Attendees:

For JTI:

- Paul Williams (Head of Corporate Affairs & Communications, JTI UK)
- Ben Townsend (Head of Government Relations, JTI UK)
- Laura Oates (Corporate Affairs Manager, JTI UK)

For DH:

- [REDACTED] (DH economist)
- [REDACTED] (DH economist)
- [REDACTED] (DH Tobacco Programme official)
- [REDACTED] (DH Legal Services)

Introduction

DH thanked JTI for their response to the consultation and noted that the focus of the meeting was to make the IA for standardised packaging of tobacco products as comprehensive and as accurate as possible. Under article 5.3 of the Framework Convention on Tobacco Control (FCTC), DH is not prohibited from meeting with tobacco companies but meetings should take place under conditions of maximum transparency. An overview minute of the meeting will be produced and placed on file once agreed between participants to the meeting and could be provided under Freedom of Information (FOI) legislation.

By way of policy background, DH reported that no advice or information had been provided to Ministers to enable them to make a decision. Ministers remained open minded about the option of standardised packaging and no communications had been made from Ministers to the tobacco team or vice versa. This was partly due to the time taken to process the vast number of consultation responses received by DH. JTI made the point that consultation responses shouldn't be basketed up into 'yes' and 'no' categories to ensure that qualitative/substantive responses are reviewed and considered appropriately, and were assured by DH that the consultation wasn't an opinion poll.

A face to face meeting was felt to be the easiest way of exploring whether JTI would be able to provide any further information to inform the IA. JTI remarked that this was the first face to face meeting with DH for a long time, indicated that the opportunity to meet face to face was appreciated and expressed the view that further such meetings would be welcome. With respect to confidentiality, the approach set out in [REDACTED]'s letter (24 Jan 2013) to JTI was reiterated. While it was acknowledged that there may be commercial sensitivities, these would be respected as far as possible within the constraints of Freedom of Information (FOI) legislation, under which exemptions exist. Any information provided in confidence would be treated as confidential. In response to any FOI request, JTI would be asked to provide reasons for non-disclosure of information and wherever possible would be involved throughout

the process. JTI noted that there were some elements in their handout which they would want redacted in response to a FOI request. DH explained that the earlier they knew about the relevant sections the better and suggested that an alternative might be for JTI to publish a redacted version on their website. DH noted that, for the purposes of the IA, the aim was to arrive at an aggregate estimate of the impact on the UK economy rather than a figure for an individual company. Of more interest than current production costs was the change in costs arising from changing packs. JTI stated that in assessing the significance of this change, all affected sectors (packaging suppliers, design agencies and retailers) must be taken into consideration.

Evolution of the market

The function of packaging in relation to price and competition was discussed. JTI explained that whilst all of their products are high quality, the packaging provides cues as to the products' price segment. Price marked packs are used to signal the price at which the product is being sold to reassure the consumer that they are getting good value. JTI went on to explain that price competition has been a feature of the market with own label brands at one time acquiring 4% of the market in multiple grocers before the growth of Sterling in the Value segment of the market, which also includes brands such as Windsor Blue and Pall Mall (retail price around £6.35 per 20). Recently, a sub-value segment has emerged with Imperial's Carlton brand replacing Red Band (Booker product) and other 'own label' brands (retail price around £5.95 for 20). The Monaco Star brand, registered to a Bulgarian firm, has also appeared in the UK market, at a price of £5.39.

Implications of standardised packaging for packaging companies

JTI explained that they currently have seven shapes of pack on the UK market with an eighth, the curve, to be introduced in March. So that DH could understand the perspective of packaging companies, JTI offered to put DH in touch with manufacturers such as Parkside Flexibles. DH noted that a meeting had already taken place with the European Carton Makers Association. JTI explained that standardised packaging would have a significant impact on the use of machinery. For example, the machinery used to manufacture the slide pack is three years old, it would be expected to be in use for many more years and if it could no longer be used as a result of regulatory change, new replacement machinery may need to be purchased. In addition, JTI said that they believed that a big impact would be felt in terms of an increase in the illicit trade, with a consequent loss of government revenue without there being any public health benefit.

The role of packaging and the illicit trade

JTI identified a link between the packaging innovation undertaken by tobacco companies over the last ten years in order to compete for existing market share and the ability of counterfeiters to imitate branded packs. When JTI acquired Gallaher in 2007, Mayfair was the leading Mid-Price brand and counterfeits began to enter the market. Subsequently, the pack has been redesigned with new colours, embossing and a blue inner foil being introduced. Recent data shows that with an average of 5 billion UK duty paid sticks of Mayfair sold in the UK in 2012, only 5 million have been seized as counterfeits. In the absence of branded packs, JTI was concerned that standardised packs would be easier and cheaper to counterfeit, making life easier and cheaper for counterfeiters while making life more difficult for consumers, retailers and law enforcement agencies to differentiate between genuine and fake packs. JTI referred to reports that they commissioned from Professors Zimmerman and Chaudhry, who provided their independent opinions on the potential impact of standardised packaging on the illicit trade in tobacco products based on their expertise in the area of illicit trade. With the B&H Silver

slide pack, no examples have been found of counterfeit packs. JTI believe that the investment required to counterfeit this type of pack is prohibitive, and hence acts as a deterrent.

JTI noted their view that findings from their empty pack survey suggest that the share of the non-UK duty paid in the market is on the rise. 766,451 empty counterfeit Amber Leaf tobacco pouches were seized in 2012 entering the UK, up from 358,244 in 2011. JTI have been informed by HMRC that large volumes of tobacco have been seized separately. JTI has engaged TNS to conduct its pack swap survey continuously for over ten years, involving 12,000 home visits.

Importance of tobacco for retailers

JTI reported that convenience, symbol groups and independents account for 68% of total retail sales of £15 billion, i.e. £10 billion at recommended retail prices. JTI noted that tobacco can account for 25% to 30% of turnover for these stores and provides vital cash flow for these businesses. Tobacco manufacturers collect approximately £1 billion per month in duty and VAT for the Government, whilst bearing approximately £1.2 billion in credit exposure each month by providing a major source of credit to their customers. JTI noted that, in addition to the revenue from the sale of tobacco products, retailers also benefit from the footfall associated with smokers.

Downtrading

JTI explained that downtrading has an impact independently of the illicit trade as there is more cash profit for retailers in Premium brands. According to the independent expert report prepared for JTI by Dr Andrew Lilico, standardised packaging could result in a few brands being left but the rest cascading to the lowest price point in the market. JTI explained that Dr Andrew Lilico would be happy to comment on his report.

Analysis by JTI indicates that if the total cigarette market in 2012 had been priced at the bottom of the Value segment (around £5.95) HM Treasury would have seen a significant fall in Government revenue – around £450 million (excise & VAT) in that year alone. However, the revenue loss could be even more dramatic – around a £810 million reduction, given the availability of substantially cheaper products now on the market (sub-value segment).

Importance of JTI to the economy

Analysis for Cogent, commissioned by the TMA, estimates that the tobacco industry accounts for 13% of gross value added (GVA) in Northern Ireland. JTI said that the public sector in Northern Ireland is equivalent to 70% of GDP with an underdeveloped private sector at 30%. JTI will invest over £265 million in its Ballymena factory between 2007 and 2015. JTI employs approximately 1,000 people in Northern Ireland and annual salaries of factory employees contribute around £57 million into the local economy each year in Northern Ireland. 50% of RYO production and 29% of cigarette production are exported.

Tobacco Products Directive (TPD)

JTI and DH agreed that standardised packaging could not be considered in isolation from the proposal to revise the TPD (the Proposal) or standardised packaging in Australia. Therefore, in assessing the impact of standardised packaging for the purpose of the UK consultation, standardised packaging in Australia and the Proposal should be reviewed carefully. DH noted that the European Commission's

proposals are subject to change depending on the views of other member states. DH explained that, while the UK Government will be represented in Brussels for the negotiations relating to the Proposal by a health attaché from the Foreign and Commonwealth Office, the attaché represents, and is briefed on, the UK Government's overall position, not just the health perspective. DH invited JTI to write with their views on the Proposal.