

EXPLANATORY MEMORANDUM FOR EUROPEAN UNION LEGISLATION/DOCUMENTS WITHIN THE SCOPE OF THE UK/EU WITHDRAWAL AGREEMENT AND THE WINDSOR FRAMEWORK

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Proposal for a COUNCIL DIRECTIVE on the structure and rates of excise duty applied to manufactured tobacco and tobacco related products (recast)

Proposal for a COUNCIL DIRECTIVE amending Directive (EU) 2020/262 as regards the general arrangements for excise duty in respect of tobacco and tobacco related products.

Submitted by HM Revenue & Customs, 10 September 2025

SUBJECT MATTER

1. On 16 July 2025 the European Commission published its proposals to update the EU's directive which currently covers tobacco excise duties and its resultant accompanying proposal to update the EU's directive that covers the general arrangements for excise duty. The measures proposed are subject to change and there is no certainty that they will come into force in their current form or at all. This EM explains the proposed changes as they are currently drafted.
2. To ensure Northern Ireland's dual access to both the UK Internal market and the EU Single Market, certain EU rules in relation to goods continue to apply under the terms of the Windsor Framework. These proposals amend or replace legislation that is listed in Annex 3 of the Windsor Framework. Consequently, the proposals have the potential to impact Northern Ireland, although it should be noted that they are at an early stage of consideration and still have potential to significantly change through the EU legislative process. The UK Government will monitor developments with these proposals and would engage with the European Commission as needed if it proves that any aspects could negatively impact Northern Ireland.
3. Current Council Directive 2011/64/EU provides harmonised EU rules that lay down the categories of tobacco product that should be subject to excise taxation, the minimum rates that member states should place on those categories, as well as some rules covering the structure of this taxation.
4. The principal proposal is to recast current Council Directive 2011/64/EU to update the rules covering tobacco products but also to extend its scope so that, besides the existing coverage of traditional tobacco products that are smoked, it also covers a number of other products that have emerged or become more significant since that directive was adopted. Therefore, the directive is also to be renamed so that it also includes tobacco related products. It also provides new minimum rates for the existing and new categories of product covered by the proposals. There is also a consequential proposal to amend Council Directive 2020/262/EU, which is the directive that covers the general arrangements for holding and moving excise goods.

This is to take account of the need to include products in those arrangements that will become excise goods under the principal proposal.

5. The European Commission note that the proposals would strengthen the EU Single Market by modernising the rules that operate in this sector. Particular emphasis is also placed on health priorities. Europe's *Beating Cancer Plan*, which has an aim to reduce tobacco use across Europe, noted that tobacco taxation is one of the most effective means to reduce tobacco use and the review of Council Directive 2011/64/EU forms part of the EU's efforts in this area. The proposals are also seen as addressing commitments to the World Health Organization Framework Convention on Tobacco Control, which recommends adoption of tax measures to reduce the demand for tobacco.
6. Besides the proposals taking account of the health consequences of traditional tobacco use, the increasing use of products that function as substitutes, such as electronic cigarettes and other emerging products, is also noted, particularly among young users. The European Commission explain that due to the emergence of such new products, and the lack of a common EU framework addressing them, a number of EU member states have introduced their own national taxes, and the absence of a common EU framework is leading to a fragmented response to the issue.
7. A key feature of the proposal is therefore to include new categories for electronic cigarettes, tobacco for heating, nicotine pouches, as well as other manufactured tobacco and nicotine products for human consumption. The one product that is intended to remain outside of the scope of the directive is Swedish Snus (Oral snuff), due to a condition of Sweden's Accession Treaty, which underlined the prohibition on sale of these products in most Member States, except for a derogation provided to Sweden. Consequently, these specific products as an exception are not to be brought within the harmonized tax framework.
8. Common definitions are proposed for each of the new categories and rules are also laid down on the structure of the excise duty charge, although for nearly all categories EU member states are offered some degree of choice as to whether reliance is more on a specific or ad valorem excise duty. This is consistent with the type of choice offered in the current Directive 2011/64/EU for existing categories.
9. In addition to the new EU minimum duty rates that are to be applied to these new categories, the proposals would also result in substantial increases to current EU minimum rates on all of the existing categories of tobacco product. The European Commission note that the current minimum rates in Directive 2011/64/EU are becoming increasingly ineffective over time, given that they have not been updated since the directive was adopted. The proposals therefore increase minimum levels but also would result in more convergence between minimum rates for different categories. The European Commission note that disparate levels of taxation between categories can lead to unintended consequences, such as product substitution. This means that, while increases are proposed on all categories of tobacco product, the proposals particularly aim for proportionately greater increases on the minimum rates for cigars, cigarillos, other smoking tobacco, waterpipe tobacco, heated tobacco and other manufactured tobacco. This would achieve a progressive convergence between the rates applied to those products and the higher rate that is set for cigarettes. In order to help achieve this, a 4-year transitional period is proposed for the categories most affected. If proposals were implemented according to suggested timescales this would run from January 2028, with a step up in the minimum that

needs to be applied halfway through the period at the end of 2029 and then final implementation of the new minimum rates by end of 2031.

10. These transitional periods are also applied to the minimum rates for the new categories of tobacco related products that cover nicotine pouches and other nicotine products.
11. No transitional periods are provided for the categories of cigarettes, fine cut tobacco for rolling of cigarettes and electronic cigarettes. The European Commission has evidently decided that transitional periods are not warranted in relation to the impacts for these particular categories.
12. As regards to liquids for electronic cigarettes, two levels of minimum rates are set, with the applicable rate being dependent on whether the product has a concentration of nicotine higher than 15mg/ml or not.
13. Part of the European Commission's proposals on the minimum rates also attempts to introduce new factors into the calculations. Currently, the minimum rates are simple nominal amounts that provide the absolute minimum level throughout the European Union and have no mechanisms of adjustment built into the directive. However, the Commission has noted that due to inflation and income growth the real value of the fixed monetary minimum rates tends to rapidly erode over time. Secondly, that diverse economic conditions such as income and price levels in the different member states mean that the purely nominal minimum rates tend to have less impact in high income countries.
14. Consequently, the proposal suggests firstly that every 3 years an adjustment is made to take account of changes to the European Union average value of the harmonised index of consumer prices over the preceding 3-year period, which uses specific data published by Eurostat. The purpose of this factor is to help the minimum rates to retain their real value over time.
15. A second new factor is also proposed that takes account of purchasing power in the relevant member state in order to fairly distribute impacts. This adjustment would take account of the Member States's Price Level Index (PLI) in comparison to the European weighted average and apply this calculation to 1/3 of the common EU rate for the category. The methodology relies on data published by Eurostat and may be regarded as complex. Recent relevant data for the UK shows a PLI factor of 124.7. Therefore, in order to calculate the minimum rate that would appear relevant to Northern Ireland, one third of the EU monetary minimum rate that is specified should be multiplied by a factor of 1.247. The sum of this would then be added back together with the other two thirds of the unadjusted monetary rate. The Commission has decided on this methodology in order to balance conclusions made by the EU Council that insisted that any future revision should take into account the specific economic situations of member states, against the risk that regularly adjusting the whole minimum rate by national purchasing power could generate large price swings that destabilise the market. Therefore, the adjustment is only to be applied to one third of the rate.
16. Besides widening the scope of the directive to include products not currently covered by Directive 2011/64/EU, the European Commission is also proposing to make particular changes to certain categories of product that are already covered by Directive 2011/64/EU. A new category for waterpipe tobacco is created. These products (shisha, hookah etc.) are currently taxed under the wider category of other smoking tobacco. However, the Commission has decided that these products merit

their own separate category, to allow for Member States to apply specific tax treatment to this type of product and to allow them to potentially monitor better what is a product sector where the level of illicit activity is particularly high. A distinction is also being made between cigars and cigarillos, which at the moment are required to be taxed at a common rate. Similarly, to waterpipe tobacco, the Commission has judged that cigarillos are a distinct enough product that the rules should allow Member States to also apply distinct tax treatment to them.

17. Another significant inclusion is that it is proposed that raw tobacco, which is the raw material for manufacture of tobacco products, would for the first time be regarded as an excise product. Raw tobacco is defined as the dried or cured form of tobacco before it is manufactured into products, so this definition would not include the activity of growing tobacco plants. The lack of controls over holding and movement of raw tobacco has been recognised as a serious weakness in the current system and there is evidence of significant numbers of illicit factories in Europe making counterfeit and other forms of illicit product. By bringing raw tobacco into the scope of excise products covered by the directives this will mean these products are subject to similar controls and supervision as other excise products. A zero minimum rate is provided for the category although member states would have the option to tax these products if they wish. However, if they do any amount paid would need to be refunded if the product is subsequently used in the manufacture of tobacco products.
18. Some less significant changes are also proposed which include technical improvements to the wording of definitions of products regarded as Cigars or Cigarillos, and removing a now superfluous exemption for product destroyed under administrative supervision, as the situations covered by that exemption are now separately covered by provisions in the current Directive 2020/262/EU.
19. The proposed changes amending Council Directive 2020/262/EU are ancillary to the main proposal. These changes are largely consequential in that they make sure that the new categories that will be covered as excise products by the main proposal are appropriately covered by the directive dealing with the general arrangements on holding and movement of goods. This means all the products will be required to move under EMCS (Excise Movement Control System) as well as covered by other administrative requirements contained in Council Directive 2020/262/EU. Including products within the scope of the requirements of this directive is proposed to ensure adequate controls of the supply-chain over taxable goods which otherwise would have a high risk to diversion or other forms of fraud. It is proposed that tobacco growers, and their associations or organisations, will be exempted provided they are not involved in the transformation of cured or dried tobacco into processed tobacco.

20. SCRUTINY HISTORY

21. No post-Brexit history on Council Directive 2011/64/EU.
22. Council Directive 2020/262/EU was subject to scrutiny as EU documents 9571/18, Com (28)346 on which HMRC submitted an Explanatory Memorandum dated 16 June 2018. The House of Commons European Scrutiny Committee reported on the Explanatory Memorandum and Directive on three occasions in reports 33 & 50, 17/19 and in report 23, 19/21 as raising issues of legal and/or political importance. The EM and Directive was sifted to the then House of Lords European Union Committee's

Financial Affairs sub-committee which did not have follow up questions for the Government.

23. MINISTERIAL RESPONSIBILITY

24. The Chancellor of the Exchequer has responsibility for United Kingdom policy on European Union monetary and economic issues, and on tax policy within the United Kingdom. The Exchequer Secretary to the Treasury has specific responsibility for excise duties.

25. INTEREST OF THE DEVOLVED GOVERNMENTS (DGs)

26. The taxation proposals contained in the Communication are a reserved matter under the UK's devolution settlements. However, this EM has been shared with NI officials to be reviewed by them, and the UK government will continue to discuss matters where relevant with each of the devolved administrations.

27. LEGAL AND PROCEDURAL ISSUES

i) Application under the Windsor Framework

28. The proposals would apply to Northern Ireland under Article 13(3) of the Windsor Framework as they amend or replace existing 'Union Acts' which fall within Article 8 and Annex 3 of the Windsor Framework. It follows that the proposals are not subject to the democratic scrutiny mechanisms set out in Article 13(3a) of the Windsor Framework and Schedule 6B of the Northern Ireland Act 1998.

ii) Legal Base

29. The proposals are based on Article 113 of the Treaty on the Functioning of the European Union (TFEU).

iii) Voting Procedure

30. Unanimity

iv) Timetable

31. The Commission propose that the new legislation would come into force from 1 January 2028. A 4-year transitional period is also provided from that time for some of the proposed increases to the EU minimum rates. At present, there is no certainty as to whether the necessary unanimity of EU member states could be achieved in order for proposals to be adopted, or that this would happen in line with the suggested timetable.

32. POLICY AND LEGAL IMPLICATIONS

33. To ensure Northern Ireland's dual access to both the UK Internal market and the EU Single Market, certain EU rules in relation to goods continue to apply under the terms of the Windsor Framework. These proposals amend or replace legislation that is listed in Annex 3 of the Windsor Framework. This means that the proposals could have the potential to impact Northern Ireland. It should, however, be noted that the proposals are not due to be implemented until 2028 and are at early stages of consideration. Their application in Northern Ireland is

still under consideration and proposals may substantively change through the EU legislative process. They will also need to be agreed unanimously by the Council of the EU (comprising EU Member States) and it is not clear that all Member States will agree to the proposals in their current form.

34. However, if implemented, some aspects of the current proposals would need to be addressed in line with our obligations under the Windsor Framework. Therefore, the Government will continue to examine the detail of these proposals as they progress through the EU legislative process and engage the European Union as appropriate through the Windsor Framework Enhanced Coordination Mechanism on VAT and Excise.
35. Much of current UK policies and legislation would remain consistent with the amended directives if these were ever implemented. However, certain elements of the current proposals appear to be out of alignment with UK legislation as it currently stands: While most of the products covered by the proposals are either currently taxed as excise products in UK, or planned to be taxed, the proposals also include certain products not treated as excise products within the UK, such as nicotine pouches and nasal snuff and there are no plans to tax these. With regards to electronic cigarettes (vaping products), the UK is currently in the process of implementing a new duty (Vaping Products Duty (VPD)) which is to be introduced from 1 October 2026. Whereas the UK will introduce a single rate of VPD, the EU proposals suggest different tax rates depending on nicotine content.
36. The new and changed definitions of some other products could also have certain limited impacts, to the extent these are not consistent with current UK legislation. In particular, tobacco for heating, waterpipe tobacco, cigars and cigarillos are all currently taxed within the UK, however if the EU proposals were implemented as they stand this could lead to specific differences to how products are categorised or described currently in UK legislation.
37. The proposal to extend the coverage of Directive 2020/262/EU to include the new categories of product within its scope is to be understood in the context of the main proposal. In particular, it would result in new administrative requirements on a number of products that are not currently subject to controls as excise goods, most notably the requirements of Excise Movement Control System (EMCS). In respect of raw tobacco, the UK does already have its own approval scheme for this product, but this product is not currently covered by EMCS requirements for the movement of excise goods. The UK is already planning on using EMCS for movements of vaping products entirely within the UK. However, as the EU currently does not recognise vaping products as an excise good, we cannot currently use EMCS to track vaping products moving from the UK to EU. The proposed amendment will resolve this issue and will reduce the burden on UK business.
38. In respect of increases to EU minimum rates, the UK already has high excise duties on tobacco products when compared to countries of the European Union. A comparison of UK duty levels against the proposed new EU minima, even when adjusted for the comparatively high price levels (PLI) in the UK, shows that UK rates

for tobacco products currently subject to excise duty are already taxed at levels well above the suggested EU minima.

39. The suggested level for vaping liquids that have high nicotine content is higher than planned UK levels of taxation announced at Autumn Budget 2024. At the end of the implementation period, it is likely that, even with yearly increases to the VPD, it will still be significantly lower than the EU minima. However, it should be underlined there is still some time before new minima would come into force and there is no current certainty that the Commission will be successful in implementing its proposals in line with the proposed timeline.
40. In general, there is likely to be far less impact of the Tobacco duty minima on Northern Ireland, than there would be in many EU member states that currently tax at significantly lower levels. For example, the European Commission estimate that the new minima on tobacco could impact 21 of 27 current member states. The suggested levels of increases to EU minima in some of what are currently the lower taxed categories, or where there is no minimum rate currently at all, appear ambitious. It is too early to know with certainty how great an obstacle the potential impacts on member states might prove to be to the European Commission obtaining the necessary unanimity to its proposals. However, if ever implemented the new minima would obviously impact on products that are not currently subject, or planned to be subject, to excise duty in the UK.
41. The following table shows the level of EU minima in comparison to current or currently planned excise duty levels in the UK. The proposed new EU minima are adjusted to take account of the new methodology proposed by the Commission that takes account of UK price levels and converted into sterling using exchange rates at time of preparation of this EM¹. This table is provided purely for illustrative purposes. Some details have been simplified for easy comparison purposes to UK. Exact calculations would also inevitably differ by time proposals could come into force.

Category	Current EU minimum rate	EU minimum rates if proposals fully implemented	Current or announced UK rate
Cigarettes	£99.38 per 1000 cigarettes	£256.28 per 1000 cigarettes	Standard rates are combination of 16.5% ad valorem excise & £334.58 per 1000 cigarettes. This equates to around £453 based on the weighted average price of cigarettes as of July 2025.

¹ Most recent UK Price Level Index for 2024 published on Eurostat has been used which shows UK Price Level Index of 124.7. Euro conversion rate of 0.864 also used. These numbers could inevitably differ by the time any proposals may come into force.

			UK <u>minimum</u> excise tax on lowest priced cigarettes is £446.67 in total per 1000 cigarettes.
Cigars	£10.34 per kg	£133.90 per kg	£417.33 per kg
Cigarillos	£10.34 per kg	£133.90 per kg	£417.33 per kg
Fine Cut Tobacco	£51.85 per kg	£201.31 per kg	£476.83 per kg
Other Smoking Tobacco	£19.01 per kg	£133.90 per kg	£183.49 per kg
Waterpipe Tobacco	£19.01 per kg	£100.19 per kg	£183.49 per kg
Heated Tobacco	Nil	£145.13 per kg	£343.91 per kg
Other manufactured tobacco	Nil	£133.90 per kg	Chewing tobacco £183.49 per kg. Nil on Nasal Snuff.
Raw tobacco	Nil	Nil	Nil
Vaping liquids <0.15 mg nicotine	Nil	£0.11 per ml	£0.22 per ml (common category for vaping liquids planned from 1 October 2026)
Vaping liquids >0.15mg nicotine	Nil	£0.34 per ml	
Nicotine pouches	Nil	£133.90 per kg or 50% of retail price	Nil
Other nicotine products	Nil	50% of retail price	Nil

42. In view of potential implications of these proposals the UK government will continue to monitor potential impacts as the proposals move through the EU legislative process. As noted, the final outcome of this process may substantially differ from these initial proposals. However, the UK government will be working to ensure that any changes do not negatively impact Northern Ireland or its position within the UK internal market.

CONSULTATION

43. The Commission carried out consultation with EU member states' administrations, businesses, public health experts, NGO's and members of the public as part of its review of Directive 2011/64/EU. The Commission has used the outputs from this to help inform the EU impact assessment that accompanied publication of these proposals.

44. There has been no UK consultation.

FINANCIAL IMPLICATIONS

45. Not applicable. Decisions on legislative proposals have not yet been made in the UK. Given that, and that there is still some uncertainty as to whether these proposals will

actually be implemented in the European Union, it would be premature to make any assessment of potential financial implications.

MINISTERIAL NAME AND SIGNATURE

A handwritten signature in black ink, appearing to read 'DM Tomlinson', written in a cursive style.

Dan Tomlinson MP
Exchequer Secretary to the Treasury
HM Treasury