

From: [REDACTED] (TRADE)

[Art. 4.1(b)]

 Ref. Ares(2017)4031279 - 14/08/2017

Sent: 2 May 2017 11:16

To: [REDACTED] (TRADE)

Subject: W: Tax discrimination in the Japanese tobacco market

Attachments: 8072013 BAT\_Japan\_Excise\_Tax\_Note.doc; Japan translation of Article 11 of the Tobacco Tax Law.docx; MOF's website for Tobacco Excise (Eng Translation).pptx

Importance: igh

From: [REDACTED]@bat.com]

Sent: Friday, July 19, 2013 9:57 AM

To: [REDACTED] (TRADE)

Cc: [REDACTED] (TRADE); [REDACTED]@bat.com

Subject: Tax discrimination in the Japanese tobacco market

Importance: High

Dear [REDACTED],

As discussed during last week's meeting, we want to bring to your attention a problem of tax discrimination in the Japanese tobacco market.

As you can see from the attached translation of the relevant provisions of Japanese law, Japan's Tobacco Tax Law (TTL) provides for a significantly reduced excise tax rate on cigarettes previously classified as Grade 3 or "Third Grade" products (see TTL, Supplementary Provisions, Art. 2). This reduced tax rate, which applies only to certain of Japan Tobacco's (JT) products closes an entire market segment from import competition and unduly discriminates against imported like products. The attached slides taken from the Japanese government's website demonstrate the clear discrimination for these listed products.

By way of background, I recall that under the monopoly system, a "Grade"-based system was adopted for cigarettes, with 56.5% of the actual tax rate being levied on Grade 1 products, 55.5% on Grade 2 products and 44.5% on Grade 3 products. At the end of the monopoly in 1985, there was a move to establish a consolidated tax rate; however, for those brands which were classified as Grade 3 products at that time, the tax rate was frozen in order to avoid burdening these Grade 3 products with a significant tax increase. Raising the tax rate on the Grade 3 products by a considerable margin was considered to be difficult given that such brands were favoured primarily by elderly people. Since this reduced tax rate is a measure that is applied only to six specific brands that were sold during the monopoly era, it is not available to the products of any manufacturer other than JT, i.e., foreign manufacturers (including our company) which have entered the market since the monopoly was abolished. These very low-priced JT products were originally expected to disappear from the market. However, they have shown the most dramatic rate of growth among all market segments, stealing market share from imported products. They currently have a more than 4% market share and are increasingly popular as a result of their price position.

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As noted during our meeting, harmonising the tax treatment for this segment would increase government revenues by 660 million USD. Furthermore, exports of cigarettes from the EU to Japan are significant both in volume and in value and there is great growth potential if the last vestiges of the monopoly period, such as this favourable tax treatment for former Third Grade products, can be rescinded.

We look forward to discussing this matter further with you and would be pleased to provide you with any additional factual or legal information you may require in order to be able to successfully raise this matter with the government of Japan.

Kind regards,

[Art. 4.1(b)]

Finally, also attached is a translation of the Minister of Finance web page on tobacco taxation. As you will note, the Minister of Finance explicitly lists the former 3rd Grade Products in Note 5.

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