



Australian Government
Australian Taxation Office

AUSTRALIAN TAXATION OFFICE

Inquiry into illicit tobacco

Parliamentary Joint Committee on Law
Enforcement

ATO Submission

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Introduction

1. The ATO welcomes the opportunity to contribute to this inquiry by the Parliamentary Joint Committee on Law Enforcement (PJCLE) into illicit tobacco. Before addressing the inquiry's terms of reference, we would like to assist the committee by providing a brief outline of the taxation of tobacco and its interaction with the customs regime.

The Regulatory Framework

2. The Commissioner of Taxation has the general administration of the *Excise Act 1901* and the *Excise Tariff Act 1921*. The *Excise Tariff Act 1921* imposes excise on relevant goods manufactured or produced in Australia and the *Excise Act 1901* deals with administrative arrangements applying to the excise system. The tobacco industry has undergone a significant restructure in the past 10 years. Licensed tobacco companies no longer grow or manufacture tobacco in Australia and therefore all legal tobacco products sold domestically are now imported.
3. Imported tobacco products are not subject to control under the *Excise Act 1901* unless they are used in the manufacture of excisable goods. Customs duty, under the *Customs Act 1901* and *Customs Tariff Act 1995*, is applied to imported tobacco products at rates equivalent to the excise duty applied to locally manufactured tobacco products. The Department of Immigration and Border Protection (DIBP) is responsible for administration of the *Customs Act 1901* and *Customs Tariff Act 1995*.
4. The Final Budget Outcome official figures¹ capture the size of the legal Australian tobacco market, with revenue obtained from customs and excise duties outlined below.

2013-14	\$8,498 Million
2014-15	\$8,848 Million
2015-16	\$9,150 Million (estimated revenue from Mid-Year Economic and Fiscal Outlook)

5. In addition to administering the collection of excise on tobacco products (alongside GST and income taxes), the ATO helps to ensure community confidence in the regulation of the legal tobacco industry by monitoring compliance with the licensing, storage, and movement of tobacco products.

Illicit tobacco

6. The DIBP is responsible for preventing illicit tobacco from being imported into Australia.
7. The ATO is responsible for detecting, investigating and prosecuting illicit domestically grown or manufactured tobacco products. As no commercial production licences have been issued since 2006, it has been illegal to grow tobacco in Australia since that time.
8. Based on the low levels of domestic illicit tobacco seizures since 2006 the ATO considers that the overall domestic production of illicit tobacco products to be small. Further, based on reported cross-border seizures of illicit tobacco, the ATO considers that illegal importations are the major source for illicit tobacco products entering domestic retail markets.

¹ www.budget.gov.au

Year	ATO seizures²	DIBP seizures³
2007-08	9.9 Tonnes	287 Tonnes
2008-09	0 Tonnes	180 Tonnes
2009-10	5.7 Tonnes	311 Tonnes
2010-11	31.1 Tonnes	258 Tonnes
2011-12	26 Tonnes	177 Tonnes
2012-13	0 Tonnes	183 Tonnes
2013-14	35 Tonnes	183 Tonnes
2014-15	16 Tonnes ⁴	150 Tonnes

Responses to the Terms of Reference

(a) the nature, prevalence and culture of illicit tobacco use in Australia, including in indigenous, regional and non-English speaking communities;

9. The ATO's intelligence focus is on the growing and movement of domestically grown illicit tobacco. The ATO identifies illicit crops by using formal networks and community tip-off information and disseminations of intelligence from law enforcement agencies.
10. Low numbers of seizures of domestically grown or manufactured tobacco and intelligence indicates that domestic illicit tobacco currently presents a small revenue risk. However this risk may grow over time if border controls become more effective. The number of illicit tobacco seizures made by the ATO and estimated excise avoided is outlined below:

Year	Seizures	Estimated excise avoided
2011-12	1	\$11.3 Million
2012-13	0	\$0
2013-14	2	\$13.4 Million
2014-15	2	\$8 Million

² Gross weight – may include wet and dry tobacco products

³ Australian Customs and Department of Immigration and Border Protection – relevant published Annual Reports 2006-2015

⁴ Two crops were seized but were ploughed in – estimated weight 16 tonnes.

(b) the role of Commonwealth law enforcement agencies in responding to the importation, use, manufacture, distribution and domestic growth of illicit tobacco;

11. For the limited amount of domestic cultivation and manufacture of illicit tobacco products detected by the ATO, we investigate and prosecute where possible. As part of this process we have seen an increasing degree of sophistication employed by the organised criminal groups who undertake this activity. For this reason there are often evidentiary difficulties in obtaining successful prosecution outcomes.
12. Having regard to the comparatively small scale of the cultivation or manufacture, the availability of evidence and the amount of resources required to achieve a successful prosecution, we may decide to seize and destroy the tobacco thereby disrupting criminal activity as an alternative to proceeding with an investigation.
13. Illicit tobacco seizures in the past year include:
 - March 2015: An excise search warrant was executed on a property at Merrigum/Kyabrum in regional Victoria. An illicit tobacco crop was found and subsequently seized and destroyed. The crop had an estimated excise value of \$4 million.
 - May 2015: An excise search warrant was executed on a property in Undera, near Shepparton, regional Victoria. An illicit tobacco crop was found and subsequently seized and destroyed. The crop had an estimated excise value of \$4 million.
14. In addition to tobacco seizures the ATO has successfully achieved a number of illicit tobacco related convictions. These include:
 - 2014: A man from western Sydney was convicted under the *Excise Act 1901* for possessing 2,000 kilograms of freshly cut tobacco leaf (equivalent to 250 kilograms of dried tobacco to which excise may be applied). He was sentenced to 9 months jail, fully suspended.
 - 2015: A man from western Sydney was convicted of two offences under the *Excise Act 1901* for growing 27,000 kilograms of tobacco (equivalent to 3,125 kilograms of dried tobacco to which excise may be applied). He was sentenced to 18 months jail, and released after serving 6 months.
 - 2015: A man from Moorabool (near Geelong in Victoria) was convicted of two offences for possessing 35,000 kilograms of tobacco leaf (equivalent to 4,361 kilograms of dried tobacco to which excise may be applied). He was sentenced to 1 year in jail, and released after serving 6 months.

(c) the loss of revenue to the Commonwealth arising from the consumption of illicit tobacco products;

15. We do not currently have an estimate of the loss of revenue arising from the consumption of illicit tobacco products. As part of the ATO's work on measuring tax gaps, a joint project with DIBP will produce a cross-agency estimate of the tobacco excise and customs duty gap. This estimate will be published in the ATO publication 'Measuring tax gaps in Australia' once it has been developed.
16. The ATO has recently partnered with an Australian university to undertake wastewater analysis of nicotine metabolites present in sewerage, in order to construct an estimate of the community's tobacco consumption in an objective manner. This data will then be analysed against the quantity

of tobacco legally sold to provide an indication of the size of the illicit tobacco market. At present this research is in its developmental phase, but if successful will likely inform the ongoing development of our illicit tobacco treatment strategy and provide greater opportunities for targeted cross agency collaboration.

(d) the involvement of organised crime, including international organised crime, in the importation, distribution and use of illicit tobacco in Australia;

17. Since commercial production licences for tobacco were withdrawn in 2006, organised criminal groups have continued to be involved in the production, manufacture and sale of illicit tobacco, however seizures and intelligence point to this being comparatively small scale. The ATO continues to see small farm plots still being used to grow illicit tobacco (primarily in Victoria) as well as the emergence of use of green houses in non-traditional tobacco growing areas.
18. In 2015, new suspects in domestic tobacco cultivation were identified indicating new players are emerging in the domestic illicit tobacco trade.
19. The ATO continues to work with DIBP, AFP and state law enforcement agencies to treat identified organised crime syndicates as part of the whole of government response. We do this by conducting criminal investigations, seizing tobacco products, sharing intelligence, raising tax assessments and supporting the Criminal Asset Confiscation Taskforce.

(e) the effectiveness of relevant Commonwealth legislation;

Proof of origin

20. Under the current legislation, successful convictions relating to the production or manufacture of illicit tobacco are difficult to obtain. This is because the place of origin of the illicit tobacco in question is required to be established in order to determine whether the offenders should be prosecuted for evasion of excise or customs duty.

Customs and excise penalties

21. Under the *Customs Act 1901*, offences for smuggling tobacco products with the intention of avoiding paying revenue were increased in 2012, and now include up to 10 years jail or financial penalties up to five times the evaded duty. By contrast, under the *Excise Act 1901* the penalties for offences relating to unlicensed domestic cultivation, manufacturing and selling of illicit tobacco have been in place since the year 2000⁵ and attract a maximum penalty of up to 2 years imprisonment or a fine which is the greater of either \$90,000 or five times the excise evaded.

(f) other related issues

22. Australia is a Party to the World Health Organisation (WHO) Framework Convention on Tobacco Control (WHO FCTC), the first treaty negotiated under the auspices of the WHO. A Protocol to Eliminate Illicit Trade in Tobacco Products (ITP) has been developed pursuant to the WHO FCTC, and if signed by Australia, would impose additional requirements to be added into Australia's regulatory framework. Some preliminary work has commenced to explore such additional requirements, for example a 'track and trace' technology used to identify and authenticate legal

⁵ *Excise Amendment (Compliance Improvement) Act 2000*

tobacco and track it through the supply chain from production to the point of sale. Given the preliminary nature of this work it is not detailed in this submission but further information can be provided to the PJCLE if requested.