

**Senate Economics Legislation Committee**

**ANSWERS TO QUESTIONS ON NOTICE**

**TREASURY**

**Australian Taxation Office**

(Budget Estimates 30 May 2006)

**Question**                    **BET 130**

**Topic:**                      **ILLEGAL TOBACCO INDUSTRY**

**Hansard page**              **Written Question**

Senator **Sherry** asked:

The Australian National Audit Office has found that \$100 million was lost in revenue through the illegal tobacco industry in Australia in 2004-2005 (Attachment A).

The ANAO report has criticised ATO for failing to confidently estimate the amount of illegal tobacco grown in Australia. Estimates, which have been described as modest, found that 347,000 tonnes of illegal tobacco was grown last financial year, a rise from 313,000 from the previous year. Despite consultation with tobacco retailers, the size of illegal crops has grown to be 1/10<sup>th</sup> of the tobacco industry. The ATO has been asked to consult more widely with associated sectors, to properly estimate the size of the illegal tobacco market.

Can you provide an overview of the ATO's current actions in relation to Australia's illegal tobacco industry?

**Answer:**

The ANAO report positively acknowledged the advances made by the Tax Office in relation to illicit tobacco. In particular the ANAO noted the improved intelligence systems, the establishment of the Serious Non Compliance business line to develop strategies around serious fraud and evasion, the shift to working across agencies in the administration of various acts, and in investigating and tracing networks involved in illicit markets.

The Tax Office uses a range of compliance activities focussing on growers and profit takers such as distributors, couriers and retailers, as well as working with the tobacco co-operatives and manufacturers as listed below.

**Growers**

The Tax Office has implemented a series of initiatives to mitigate the risks of tobacco entering the illicit market. These include:

- applying a whole-of-tax approach to the tax affairs of individuals and entities identified as being high risk growers;
- continued improvements to probity checks for new licence applications;
- implementation of recent legislative changes, commencing on 1 July 2006, including a three year review of all licences;
- implementation of a rigorous review process for all new licences and renewals;
- licences being subject to a strong regime of conditions designed to ensure a greater level of compliance with the Excise Act;

## **Senate Economics Legislation Committee**

### **ANSWERS TO QUESTIONS ON NOTICE**

#### **TREASURY**

##### **Australian Taxation Office**

(Budget Estimates 30 May 2006)

- monitoring and enforcement of licence conditions;
- a visible presence in the growing areas conducting both planned and unannounced visits to growers throughout the growing season;
- the use of aerial photography to monitor and locate illegal crops;
- continuing to work closely with growers and their co-operatives to assist them to meet their obligations; and
- investigating new technology.

#### **Distribution Networks**

The Tax Office will continue its focus on identifying and disrupting the distribution networks associated with illicit tobacco. This is part of a multi-layered approach which focuses on dealing with illicit tobacco at the source, distribution and retail points. We will continue to focus on:

- seizure of illegal tobacco, vehicles and threshing equipment before tobacco enters the illicit market;
- joint operations with Customs and other law enforcement agencies designed to identify and disrupt the distribution of illicit tobacco; and
- prosecution of offenders.

#### **Retailers**

Our activities include:

- conducting compliance activities on retailers;
- informing and educating retailers of their obligations; and
- issuing penalty infringement notices or prosecuting offenders found to be breaching the Excise Act.

#### **Manufacturers and the Victorian and South Queensland tobacco co-operatives**

The Tax Office continues to:

- work in collaboration with each group to develop compliance strategies and ensure they understand their own obligations under the Act;
- work closely with them in relation to emerging issues that impact on their growers;
- ensure an on-going consultative approach is adopted to the development of new licence conditions; and
- continue to support the strong partnerships built up through the consultative forums with key industry stakeholders.

# Senate Economics Legislation Committee

## ANSWERS TO QUESTIONS ON NOTICE

### TREASURY

#### Australian Taxation Office

(Budget Estimates 30 May 2006)

#### Outcomes of this activity

The Tax Office continues to work with stakeholders to ensure that the risk of tobacco being diverted to the illicit market is mitigated. Some of the outcomes to date include:

- in December 2005, a Tax Office-initiated multi-agency team involving 250 staff from the Tax Office, Customs, Australian Federal Police and Victoria Police executed warrants on a range of entities allegedly associated with the illegal market with the aim of disrupting the illicit tobacco distribution network and resulted in:
  - 24 prosecution briefs being referred to the Commonwealth Director of Public Prosecutions (CDPP); and
  - 33 penalty infringement notices being issued.
  
- Other operations have resulted in the finalisation of 57 prosecutions. These prosecutions resulted in;
  - 20 offenders receiving jail sentences;
  - 34 offenders receiving non custodial sentences including substantial fines;
  - 3 cases being dismissed; and
  - the referral of 89 briefs of evidence to the CDPP and the Australian Government Solicitor.
  
- In 2005-06, the Tax Office seized 18,015 kilograms of cut and leaf tobacco, 9 motor vehicles and 22 tobacco cutting machines. Court outcomes resulted in \$1,252,218 in fines and \$156,981 in reparation orders.
  
- From 1 July 2002 to 31 August 2006, the Tax Office has seized approximately 172,400 kilograms of cut and leaf tobacco, over 200,000 tobacco plants, 75 cutting machines and 92 vehicles. In the same period, excluding the process of closing down the North Queensland growing region, the Tax Office has cancelled 12 licences.

1. *Can you explain why it has been difficult for the ATO to accurately estimate the amount of revenue lost through the illegal tobacco industry every year?*

#### **Answer:**

As acknowledged in the ANAO report there are a number of limitations in the data available to estimate the size of the illicit tobacco industry. Due to the covert nature of the illegal tobacco industry, reliable statistics cannot be obtained nor reasonably estimated. There is a range of indirect indicators that may be used to estimate the size of the illicit tobacco industry including:

- comparing predicted tobacco crop yields with the amount of tobacco sold on the legal market; and
- the amount of cigarette papers and tubes imported into Australia.

## Senate Economics Legislation Committee

### ANSWERS TO QUESTIONS ON NOTICE

#### TREASURY

##### Australian Taxation Office

(Budget Estimates 30 May 2006)

These indicators are dependent on many variables and are very sensitive to assumptions. The number of imported tubes and cigarette papers does not differentiate between those used for legal tobacco, illicit tobacco and illegal drug use. Advice from the tobacco manufacturers has been that there have been increased sales of loose tobacco which will also likely impact on the number of tubes used.

The use of crop yields has issues regarding variations. These variations, as with all primary production, can impact across a whole region or sub-region due to general seasonal variations and conditions. There are also variations based on the skill of the producer and the ability to control disease. However the use of crop yields is effective for benchmarking and therefore targeting higher risk growers.

2. *How do you seek to overcome this problem with estimating the revenue lost?*

**Answer:**

The Tax Office continues to improve risk identification processes to ensure that resources are directed appropriately through continually developing, evaluating and updating strategies to improve effectiveness. This approach was supported by the ANAO. The indicators include monitoring and analysis of:

- the amount of legal tobacco grown;
- legal cigarette sales;
- the demographics of smokers in Australia;
- the price of illegal tobacco;
- industry trends and intelligence; and
- revenue collection.

3. *Figures show the number of illegal tobacco crops continues to rise – at a time when the ATO is aware more than ever about the problem. How do you explain this?*

**Answer:**

The ANAO recognised that there is a range of uncertainties inherent in estimates of the quantities of tobacco legally grown and illegally diverted. The evidence to date suggests that the supply into the illicit market is from both local producers and through imported product.

The Tax Office undertakes surveillance and investigates any reports of illegal tobacco growing and will continue a multi-agency approach to identify if illicit tobacco seized is domestic or imported. The Tax Office has officers permanently located in the Victorian growing region as well as an expanded workforce throughout the production season. By working in cooperation with the Victorian Police in the Myrtleford area, action is taken to intercept vehicles where it is believed tobacco is being unlawfully transported.

**Senate Economics Legislation Committee**

**ANSWERS TO QUESTIONS ON NOTICE**

**TREASURY**

**Australian Taxation Office**

(Budget Estimates 30 May 2006)

The Tax Office continues to work closely and share intelligence with Customs, the Australian Federal Police and State police forces to develop appropriate strategies to combat the illicit trade. It should be noted that Customs has responsibility for dealing with imported tobacco and tobacco products including illicit cross border activity.

4. *Would it be accurate to say that the only way to make in roads (sic) into the illegal tobacco industry, is to encourage people not to smoke?*

**Answer:**

There are a range of strategies needed to address this issue. The ANAO also supported the continuation of the range of strategies employed by the Tax Office to combat the illegal tobacco industry.