

Parliament of the Commonwealth of Australia

**SENATE ECONOMICS LEGISLATION
COMMITTEE**

**CONSIDERATION OF LEGISLATION
REFERRED TO THE COMMITTEE**

Excise Amendment (Compliance Improvement) Bill 2000

August 2000

Commonwealth of Australia

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SENATE ECONOMICS LEGISLATION COMMITTEE

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REPORT

Reference of the Bill to the Committee

1.1 The Excise Amendment (Compliance Improvement) Bill 2000 was introduced into the House of Representatives on 21 June 2000. Following a report by the Selection of Bills Committee, the Senate referred the Bill to this Committee on 28 June 2000 for examination and report by 16 August 2000.¹ In its report, the Selection of Bills Committee requested that an opportunity be given for public comment on the provisions of the Bill.

The Committee's Inquiry

1.2 The Committee identified a number of parties with a potential interest in the Bill, advised them of the inquiry, and invited them to participate. Additionally the inquiry was advertised on the Parliament website. The Committee received 3 submissions to the inquiry (see Appendix 1).

1.3 The Committee held a public hearing on the Bill in Melbourne on 4 August 2000. The witnesses who appeared at the hearing are shown in Appendix 2.

Measures in the Bill

1.4 The Bill proposes to amend the *Excise Act 1901* to counter the growing trade in illegal tobacco, known as chop chop, which is estimated to be worth over \$300 million a year in lost excise revenue. To this end the Bill establishes a comprehensive licensing system for the growing, transporting, trade, manufacture and storage of tobacco. In addition, the Bill contains provisions which will require the individual labelling of tobacco bales. The Bill also deals with the manufacture and storage of excisable goods generally.

1.5 The proposed legislation contains provisions which expand the search powers of officers. The new powers would allow searches of conveyances at any place, without warrant, if officers have reasonable grounds to believe that the conveyance holds tobacco leaf or excisable goods.

1.6 The Bill increases the penalty for the unlawful movement or possession of goods where the duty has not been paid. The maximum fine will be set at 500 penalty units (currently \$55 000) or five times the duty payable. In addition to fines, the Bill provides for a maximum term of up to two years imprisonment.

1 Selection of Bills Committee Report No. 10 of 2000, dated 28 June 2000.

Comparison of key features of new and current law²

New law	Current law
Growing tobacco will be regulated. Only a licensed producer will be permitted to produce tobacco seed, plants and leaf.	Existing controls are limited to the regulation of tobacco leaf after it has been stripped from the plant.
Permission will be needed to move tobacco leaf. An identification label will need to be attached to bales of tobacco leaf prior to their movement from a producer's premises unless there is an express permission for movement without a label.	The movement of tobacco leaf is not regulated.
Conveyances will be able to be stopped and searched for excisable goods or tobacco leaf at any place.	Only conveyances which are about to leave a factory or other 'excise place' may be stopped and searched, and only for excisable goods.
A two-tier structuring of some offence provisions which provide for increased maximum penalties, including a two year maximum term of imprisonment, where the requisite mental element is established.	Current penalties for some offences have no deterrent effect because they are small relative to the potential proceeds from illegal activity.
Introduction of pecuniary penalties for the offence of unauthorised movement of tobacco leaf and the counterfeiting of tobacco bale labels.	There are no controls on the movement of tobacco leaf.
Introduction of a fixed 20 penalty units infringement notice penalty for selling or possessing tobacco on which duty has not been paid.	No infringement notice scheme.
Increase the maximum penalty to 500 penalty units for existing offences dealing with the movement of excisable goods without authority or permission.	Current maximum penalty – usually \$5,000.
<p>Comprehensive scheme for the granting, suspension and cancellation of licences for:</p> <ul style="list-style-type: none"> • producing or dealing in tobacco seeds, plant or leaf; and • manufacturing and storing excisable goods. 	There is no basis for refusing an application for registration as a <i>producer</i> or <i>dealer</i> or for the declaration of an <i>approved place</i> as a place for storing excisable goods. There is very limited scope for suspending or cancelling a manufacturing licence.

Issues Raised in Evidence

1.7 The Committee received submissions and additional information from several major manufacturers of tobacco products. Most of these submissions supported the legislation. The main issues raised in evidence related to health issues, the impact of punitive taxes, loss of excise revenue and adequate resourcing to counter the chop chop industry.

Revenue cost

1.8 Submissions made by tobacco manufacturers highlighted the cost of the illegal tobacco industry, with conservative estimates ranging from \$400 million³ to \$600 million⁴ annually. This translates into a loss of excise revenue of over \$300 million⁵ annually. Another financial impact of the illegal trade is the loss of income to the legal tobacco industry. This loss is estimated to be around \$120 million,⁶ which includes losses to manufacturers, wholesalers and retailers.

1.9 Some witnesses estimated that if the chop chop industry remains unchecked it could reach sales of 2000 tonnes by December 2000.⁷ Such dramatic growth would place pressure on legitimate retailers to sell chop chop in order to be competitive in the market place.

Impact of taxes

1.10 Several witnesses and submissions criticised the impact of the current levels of taxing of tobacco products, stating that high taxes are driving the illegal industry. The Committee noted that 118 grams (210 cigarettes) of legal tobacco in the form of ready rolled cigarettes retails for \$66.50, this includes a tax component of \$47.35, whereas a similar amount of loose leaf illegal tobacco retails for \$5.90.⁸ Some witnesses argued that the current levels of 'punitive' taxes are creating an environment which allows the illegal trade in tobacco to flourish. According to these witnesses regular tax increases aimed at reducing smoking numbers are simply driving more smokers to opt for the cheaper chop chop product.⁹

1.11 Evidence given by British American Tobacco Australasia (BATA) suggested placing a tax on the pre-rolled empty cigarette filter papers, known as tubes. BATA stated that most of the one billion tubes imported annually are used to produce pre-rolled chop chop cigarettes. However, Philip Morris stated that tubes are also used by legal roll-your-own smokers, so any tax on tubes would discriminate against that group. In the Committee's view a tax on tubes may compound the chop chop problem by encouraging smokers to switch to cheaper substitute material to produce cigarettes.

3 Submission No. 1, p. 4

4 Submission No. 3, p. 1

5 Evidence, p. 21

6 Submission No. 3, p. 1

7 Submission No. 3, p. 1

8 Evidence, p. 21

9 Evidence, p. 21

Health issues

1.12 The unregulated sale of chop chop bypasses government health regulations and manufacturing standards. Consequently, sales of illegal tobacco have no health warnings on the packaging and avoid controls over tar and nicotine levels and other additives. The lack of regulation on the sale of chop chop also makes it more readily available to children through mail order outlets or other unregulated channels, making it a significant risk to community health.

Industry involvement

1.13 Witnesses claimed that the main supply of tobacco leaf for the chop chop industry is from legitimate growers, who supply both the legal and illegal industries.¹⁰ These growers are attracted by the higher prices paid by the illegal manufactures for tobacco leaf (\$10 to \$20 per kilo as opposed to \$6 per kilo paid by legal manufacturers). The Committee noted that this nexus between the illegal and legal trade provides an opportunity for legitimate manufactures to assist in monitoring tobacco production, by predicting the crop yields of their growers. These estimates could help authorities to identify the origins of tobacco supplied to the illegal trade.

1.14 The Committee also noted other efforts that the legal industry is making to counter the chop chop industry. These include attempting to remove as much tobacco from the market place as possible by purchasing all tobacco put up for sale. In addition, Philip Morris is developing tests which would enable its laboratory to pinpoint the origin of tobacco.

Opposition to the Bill

1.15 The submission from Oztobacco, an internet marketer of Grow Your Own Tobacco Kits, stated that the new measures would close their business, presumably because the excise would make them uncompetitive. Oztobacco indicated that the market for kits within Australia is relatively small: 93 kits were sold in 1999-2000 financial year.¹¹

1.16 Oztobacco appeared to base its argument on the assumption that its business was currently operating within the law, even though it seems not to be paying excise. The ATO indicated that Oztobacco's view was wrong. The ATO stated:

Contrary to assertions in [Oztobacco's] submission, growing, drying and cutting your own tobacco is not a legitimate activity. There is no tobacco equivalent to the do-it-yourself concession that applies to home brewers under the Excise law.

Easy access to tobacco seed presents a high risk that any non-commercial growing and manufacture of tobacco could easily transform into commercial activity outside the licensed sector. This would undermine the revenue and health policies of the Government in relation to tobacco.

On enactment of the Bill, the ATO proposes to inform Mr Groves that he will no longer be able to sell tobacco seed.¹²

10 Evidence, p. 23

11 Submission No. 2, p. 1

12 Correspondence from ATO, 11 August 2000.

Industry Support of New Measures

1.17 During the hearings Philip Morris, BATA and other witnesses expressed strong support for the Bill. These bodies forecast that the Bill would not wipe out the problem of illegal tobacco but was a step in the right direction. However, the same witnesses raised concerns that for the legislation to make an impact it would need to be adequately resourced:

As I said, everybody involved in policing this needs to be better resourced. We need to have more people on the ground. If you can capture some of that \$300 million in revenue, there are adequate funds around to provide these resources.¹³

1.18 In response the ATO pointed out that they will be expanding their capability by an extra 85 investigators, primarily concerned with the tobacco industry.¹⁴ The Committee is of the view that the success of the new measures will also require the support and expertise of the industry, particularly in areas such as crop monitoring and other jointly funded projects. The Committee encourages the industry to extend such assistance to government agencies in stamping out the chop chop industry.

1.19 The Committee is of the view that the most effective point at which to successfully counter the illegal trade in tobacco is at the growing stage. The Committee encourages both government and industry to investigate methods of better monitoring crops and predicting yields, similar to surveillance used in the poppy industry in Tasmania.

Recommendation

1.20 The Committee recommends that the Senate pass the Bill.

Senator the Hon Brian Gibson
Chairman

13 Evidence, p. 25

14 Evidence, p. 32

APPENDIX 1**LIST OF SUBMISSIONS**

- No. 1 Philip Morris Limited
- No. 2 Oztobacco
- No. 3 British American Tobacco, Australasia

APPENDIX 2**LIST OF WITNESSES
APPEARING BEFORE THE COMMITTEE****Friday, 4 August 2000**

Australian Institute of Management
181 Fitzroy Street, St Kilda

Philip Morris

Mr John Scott, Managing Director

British American Tobacco

Mr Brendan Brady, Corporate and Regulatory Affairs Director

Australian Taxation Office

Mr Bruce Thomson, Assistant Commissioner
Mr Wil Duda, Instructing Officer