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The Treasury  
Langton Crescent  
PARKES ACT 2600

Trade Revenue Policy  
Department of Home Affairs  
5 Chan Street  
BELCONNEN ACT 2617

By email [tobacco@treasury.gov.au](mailto:tobacco@treasury.gov.au);  
[traderevenue@homeaffairs.gov.au](mailto:traderevenue@homeaffairs.gov.au)

**Public Consultation Submission on Collecting Tobacco Duties and Taxes at the Border**

- *Excise Laws Amendment (Collecting Tobacco Duties at Manufacture) Bill 2018 (Exposure Draft)*
- *Excise Tariff Amendment (Collecting Tobacco Duties at Manufacture) Bill 2018 (Exposure Draft)*
- *Customs Amendment (Collecting Tobacco Duties at the Border) Bill 2018 (Exposure Draft)*

Tobacco Imports Pty Ltd (TIC) is an importer of tobacco in cigarette form. TIC wishes to thank The Treasury and the Department of Home Affairs for the opportunity to make this submission on the proposed changes to the above laws arising from the Government's policy decision to collect tobacco duties and taxes at the border.

We acknowledge that the decision to collect tobacco taxes and duties at the border is part of a package aimed at combatting illicit tobacco. TIC wishes to voice its concern and condemnation of the trade in illicit tobacco, which diverts duties from the Government and business from legitimate and lawful importers, such as TIC.

TIC makes this submission to both The Treasury and the Department of Home Affairs due to the interaction between the activities and processes that they administer (jointly and separately), arising from the classification of tobacco imports as Excise Equivalent Goods (EEG) and resulting in their import duty treatment mirroring what would be the excise treatment for any Australian-manufactured tobacco. TIC's submissions therefore relate to each of the above Exposure Draft Bills.

Whilst supportive overall of the initiatives to combat illicit tobacco, TIC is concerned that the proposed measures will immediately, materially and detrimentally impact tobacco importers, in particular smaller and medium businesses, such as TIC. The result will be almost unbearable financial pressures on such businesses, which poses risks to their continued operation and, therefore, the continued employment of Australian workers and ongoing financial contribution to the broader economy.

For these reasons, TIC is of the view that transitional concessions must be made during the introduction of the above new laws, so that the numerous small and medium businesses which make up the 'other' segment of the Australian tobacco market<sup>1</sup> are not forced out of business or otherwise subjected to unbearable financial strain as the direct result of the introduction of the new laws.

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<sup>1</sup> As opposed to the three largest tobacco companies which together comprise some 84.7% of the Australian tobacco market.



A Locked Mail Bag 1002  
Shellharbour City  
NSW 2529 Australia

9 Durgadin Drive,  
Albion Park Rail  
NSW 2527 Australia

T 1300 5655 2727

E [sales@tobaccoimportscompany.com.au](mailto:sales@tobaccoimportscompany.com.au)

In order to avoid this inequitable and potentially market-distorting financial hardship, small and medium businesses should be exempt from the new requirements.

Alternatively, proper transitional arrangements should be put in place to preserve the status quo and not penalise businesses for engaging in current proper and lawful conduct. For existing warehouse stock, the effective date of the new laws should be deferred for 12 months, to 1 July 2020, to allow the orderly reduction of underbond stock in the usual course of business.

Alternatively, small and medium businesses should automatically be granted payment plan terms, which should be exempt from interest and any requirement to provide security for those payment plans.

Without these measures, the new laws will dramatically and detrimentally affect the small and medium businesses which, together and separately, form a vital competitive counterpoint to the three large international businesses which comprise the remaining 98% to 99% of the Australian cigarette import market.

### **1. The requirement for importers to pay full duty immediately upon the arrival of goods in Australia will place unbearable financial strain on businesses, in particular smaller to medium businesses**

Presently, importers are able to enter tobacco products under bond into licensed warehouses for storage, prior to entering the goods for home consumption. Duty is only payable upon entering the goods for home consumption.

This practice is long-established, lawful and legitimate. This practice results in a delay or deferral of the payment of duty from the time that the goods arrive in Australia. This delay or deferral is appropriate, given that approximately 60% of the total sales price of cigarettes is comprised of duty or tax,<sup>2</sup> meaning that profit margins in the tobacco sector are very low and cash flow management (more closely aligning the payment of taxes and duties with the actual receipt of payment from the sale of goods) is critical to survival.

This practice does not result in some 'win' or 'freedom' for tobacco importers as opposed to other sectors. Warehoused goods are subject to strict physical control and security arrangements, including restrictions on movement, reporting and audit requirements, and cannot be sold until they are entered and duty paid.

This practice will be abolished under the new laws and importers will have to pay duty on imports immediately upon their arrival in Australia. Duty represents approximately 91% of the importer's sales price for the goods, meaning that importers will now have to fund costs of 91% of their gross revenue in advance, before the goods are sold and payment received.

A Locked Mail Bag 1002

Shellharbour City  
NSW 2529 Australia

9 Durgadin Drive,  
Albion Park Rail  
NSW 2527 Australia

T 1300 5655 2727

E [sales@tobaccoimportscompany.com.au](mailto:sales@tobaccoimportscompany.com.au)

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<sup>2</sup> Scollo, M, Bayly, M., *13.9 Future directions for reform of tobacco taxes*, in Scollo, MM and Winstanley, MH [editors], *Tobacco in Australia: Facts and issues*, Melbourne: Cancer Council Victoria; 2016, available from <http://www.tobaccoinustralia.org.au/chapter-13-taxation/13-9-future-directions-for-reform-of-tobacco-taxes>.

Importers, particularly those small and medium businesses in the 'other' category and comprising 1% to 2% of the Australian cigarette market (including TIC) will likely need to establish new finance facilities to fund the advance payment of duty. Those new finance facilities will come at a cost (interest). Given the high value but low profit of tobacco products, the cost of funding such financing facilities has the potential to wipe out importers' net profit before income tax *entirely*, immediately rendering those businesses unprofitable. Summary details of the financial impact on TIC are included in a separate, confidential attachment.

**A** Locked Mail Bag 1002  
Shellharbour City  
NSW 2529 Australia  
9 Durgadin Drive,  
Albion Park Rail  
NSW 2527 Australia  
**T** 1300 5655 2727  
**E** sales@tobaccoimportscompany.com.au

**2. The requirement to enter all existing warehoused tobacco on 1 July 2019 and immediately pay all duty or provide security for the duty within 7 days will place unbearable financial strain on businesses, in particular smaller to medium businesses**

Separate to the general financial burden imposed on smaller and medium importers such as TIC by the introduction of the new laws, the application of the new laws retrospectively to existing imported goods will place a further unbearable financial burden on importers.

Under the draft laws, any existing warehoused stock as at 1 July 2019 must be entered for home consumption on 1 July 2019 and duty paid or security provided within 7 days. Maintaining sufficient warehoused stock in Australia is a necessary operating requirement of the tobacco importing business, in order to manage supply and meet fluctuating weekly and monthly demand and customer delivery requirements. Indeed, stored stock levels are often a requirement contained in ongoing customer tobacco supply arrangements. So, as at 1 July 2019, it is inevitable and part of the responsible and effective running of a tobacco import business that importers will have not insubstantial warehoused stock on hand.

Requiring importers to enter that stock immediately upon 1 July 2019 and pay duty or provide security within 7 days will not be manageable. The advance duty on this existing stock will not be paid over time but will have to be paid in one hit. For many small to medium businesses, including TIC, this could be a 'king hit'.

We acknowledge preliminary discussions with representatives of the Australian Taxation Office (ATO), Indirect Tax Department to the effect that smaller and medium importers faced with such insurmountable financial pressure may be able to enter into 12 month payment arrangements.

However, if the ATO agrees to enter into any such payment plan (which is discretionary and not available as of right):

- Interest will accrue on the 'overdue' debt,<sup>3</sup> and
- Security for the full amount of the 'overdue' debt is generally required to be maintained for the duration of the payment plan.<sup>4</sup>

The additional cost of these requirements, jointly and separately, means that any 'relief' provided by the payment plan may be illusory, or only very partial.

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<sup>3</sup> <https://www.ato.gov.au/General/Paying-the-ATO/Help-with-paying/#Onlineandautomatedpaymentplans>.

<sup>4</sup> <https://www.ato.gov.au/General/Paying-the-ATO/Help-with-paying/#Securedpaymentplan>.



If a business is required to give a security, it must still fund that security. The ATO's preferred securities are a registered mortgage over freehold property or an unconditional bank guarantee from an Australian bank.<sup>5</sup> The freehold mortgage can be disregarded, as it won't be an option for most businesses. As a condition of granting an unconditional bank guarantee, any Australian bank will require counter-security for the full amount of the guarantee.

If an importer has stock equating to duty owing of \$20 million as at 1 July 2019, before any Australian bank will agree to provide a guarantee that is a condition of the ATO accepting any payment plan, the importer will have to provide \$20 million counter-security to the bank. So, even if a payment plan is accepted by the ATO, the importer will still need to fund the total duty payment effectively immediately and in one 'king hit' within 7 days of 1 July 2019. Further, the importer will have to maintain that full security for the full 12 month term of the payment plan, despite the cumulative payment of duty each month. Further, interest will accrue to the ATO on the 'overdue' debt. Summary details of the financial impact on TIC are included in a separate, confidential attachment.

**A** Locked Mail Bag 1002  
Shellharbour City  
NSW 2529 Australia  
9 Durgadin Drive,  
Albion Park Rail  
NSW 2527 Australia  
**T** 1300 5655 2727  
**E** sales@tobaccoimportscompany.com.au

### **3. The almost unbearable financial burden arising from the obligation to pay duty in advance and pay or secure duty on all warehoused stock as at 1 July 2019 will be felt unequally by small and medium businesses, with likely market-distorting effects**

Three major tobacco importers control the vast majority of the Australian tobacco market, holding 84.7% of the overall tobacco market<sup>6</sup> and approximately 98% to 99%<sup>7</sup> of the Australian cigarette market (the market in which TIC participates). The size and scale of those businesses means that they will be more able to fund the impact of the advance payment of duty generally and the mandatory entry of and payment of duty on existing warehoused tobacco goods on 1 July 2019. The other numerous small to medium businesses comprising the remaining 1% to 2% of the market will be disproportionately affected by this impost, impeding their ability fairly to compete in the market and potentially jeopardising their operations.

The inequitable impact of the taxation regulatory burdens placed on small to medium tobacco businesses, such as TIC, has been recognised by the ATO. In its submission to the Senate Select Committee on Red Tape, speaking in relation to the imposition of import quotas, the ATO stated that *"due to the administrative costs...on these smaller entities"* the ATO sought not to impose heavily on small to medium importers, so that *"the potentially distorting effects on entities competing in the same market are removed"*. Speaking more generally (not just in relation to quotas), the ATO acknowledged that its *"responsibility [is] to administer the revenue effectively and not [impose] unreasonably upon duty payers"* and, in that interest, to take *"as minimalist an approach as possible*

<sup>5</sup> Ibid.

<sup>6</sup> Scollo, M, Bayly, M., *10.3 The manufacturing and wholesaling industry in Australia—major international companies*, op. cit., available from <http://www.tobaccoaustralia.org.au/chapter-10-tobacco-industry/10-3-the-manufacturing-and-wholesaling-industry-in-australia>.

<sup>7</sup> The Parliament of the Commonwealth of Australia, House of Representatives, *Customs Tariff Amendment (Tobacco) Bill 2016, Explanatory Memorandum* at [2.102]; Australian Taxation Office, *Submission – Inquiry into the effect of red tape on tobacco retail*, 2017 at [36], available at [https://www.aph.gov.au/Parliamentary\\_Business/Committees/Senate/Red\\_Tape/Tobacco/Submissions](https://www.aph.gov.au/Parliamentary_Business/Committees/Senate/Red_Tape/Tobacco/Submissions); KPMG, *Illicit tobacco in Australia, 2017 Full Year Report*, 20 April 2018, available at <https://home.kpmg.com/uk/en/home/insights/2018/05/illicit-tobacco-in-australia-2017.html>; The Auditor-General, Australian National Audit Office, ANAO Audit Report No. 34 2015-2016, *Administration of Tobacco Excise Equivalent Goods – Australian Taxation Office and Department of Immigration and Border Protection*, 2016 at [4.6], available at [https://www.anao.gov.au/sites/g/files/net4981/f/ANAO\\_Report\\_2015-2016\\_34.pdf](https://www.anao.gov.au/sites/g/files/net4981/f/ANAO_Report_2015-2016_34.pdf).

*to still achieve the intended outcome” by adopting approaches “that endeavour to minimise compliance and administrative costs while still achieving the desired regulatory and legislative outcomes”.*<sup>8</sup>

The importance of avoiding the unequal and distorting impact of the administration of duty regulation on the smaller and medium importers, including TIC and other importers comprising the 1%-2% balance of the cigarette market, has been endorsed by the Senate Select Committee on Red Tape. In its interim report on the effect of red tape in the tobacco industry, the Red Tape Committee recognised the “*high levels of regulation that adversely affect small businesses which retail legal products*”, shared its view that “*a market operates most efficiently when there is limited regulation which has clearly identified policy objectives*” and recommended that “*all governments review their tobacco control measures and identify opportunities to refocus it and reduce red tape burden on small retailers*”.<sup>9</sup>

**A** Locked Mail Bag 1002  
Shellharbour City  
NSW 2529 Australia  
  
9 Durgadin Drive,  
Albion Park Rail  
NSW 2527 Australia  
**T** 1300 5655 2727  
**E** sales@tobaccoimportscompany.com.au

The Red Tape Committee’s conclusions should be viewed in context and are not limited only to those businesses defined as “small businesses” within the meaning of the ATO tax concessions. They are applicable to the small and medium enterprises that form the 15.3% balance of the total Australian tobacco market and 1% to 2% balance of the Australian cigarette market,<sup>10</sup> including TIC. Further, when considering the impact of duty administration and payment arrangements on small and medium businesses in the tobacco sector, it must be remembered that approximately 91% of the imported sale price of cigarettes represents duty and not below the line revenue – so businesses which might not technically qualify as small business under tax concession rules can still in fact be businesses with very small non-tax revenue. A summary of TIC’s financial size is included in a separate, confidential attachment.

#### **4. Policy and legislation should be administered to protect revenue, not penalise duty payers; the imposition of any new measures imposing burden on business must be evidence-based and risk-targeted**

Taxation administration measures, particularly those that are punitive or have a potentially punitive impact, should be exercised only to the extent necessary to protect and not in a manner which penalises duty payers or exposes them to undue financial burden. For this reason, it has been recognised that the imposition of any administrative burden or revenue control measures should only be done where directly supported by clear evidence- and risk-based assessments.

This approach to combatting the illicit tobacco trade has been sanctioned by Parliament, which supports a “*risk-based intelligence-led approach to focus on the high risk areas of non-compliance*”<sup>11</sup> in the area of illicit tobacco. Further, the need for any administrative or regulatory intervention to meet this threshold has been recognised as a significant issue in reducing regulatory burden and red tape for small and medium businesses, such as TIC, with the Red Tape Committee recommending

<sup>8</sup> Australian Taxation Office, *Submission – Inquiry into the effect of red tape on tobacco retail*, op. cit. at [36, 38, 48, 49 and 54], available at [https://www.aph.gov.au/Parliamentary\\_Business/Committees/Senate/Red\\_Tape/Tobacco/Submissions](https://www.aph.gov.au/Parliamentary_Business/Committees/Senate/Red_Tape/Tobacco/Submissions).

<sup>9</sup> The Senate Select Committee on Red Tape, *Effect of red tape on tobacco retail, Interim report*, June 2017, at [2.56], available at [https://www.aph.gov.au/Parliamentary\\_Business/Committees/Senate/Red\\_Tape/Tobacco/Interim\\_Report](https://www.aph.gov.au/Parliamentary_Business/Committees/Senate/Red_Tape/Tobacco/Interim_Report).

<sup>10</sup> Ibid, at heading to [2.16].

<sup>11</sup> The Parliament of the Commonwealth of Australia, House of Representatives, *Customs Tariff Amendment (Tobacco) Bill 2014, Explanatory Memorandum* at [2.103]; The Parliament of the Commonwealth of Australia, House of Representatives, *Customs Tariff Amendment (Tobacco) Bill 2016, Explanatory Memorandum* at [2.71].



that the Commonwealth government review its tobacco control measures, with a view to “*identifying and eliminating regulatory measures that are not evidence-based*”.<sup>12</sup>

The risk identification and assessment relating to illicit tobacco has not been properly or consistently assessed by the government agencies responsible for tobacco duty administration. An independent audit into the administration of tobacco excise equivalent goods conducted by the Australian National Audit Office found that “*risks associated with the administration of tobacco excise equivalent goods have not been consistently assessed. Fluctuations in the annual risk rating (from ‘low’ to ‘moderate’ to ‘significant’) lacked a clear rationale, with the most recent rating based on reputational risk to the ATO and DIBP*” (emphasis added).<sup>13</sup>

Furthermore, there is some suggestion that the proposed measures, focused on the further regulation of the EEG regime, are not in fact directly relevant to the control of the illicit tobacco market, with the predecessor to the Department of Home Affairs stating “[w]hile illicit tobacco presents complementary risks, these do not directly impact the administration of the EEG regime. The Department believes the illicit tobacco market is not indicative of the effectiveness of EEG administration by either the ATO or the Department”.

As a result, there is an argument that the imposition of the new measures is misdirected, burdening certain participants within the tobacco market with additional controls which are disproportionate to the risks objectively posed by those participants.

The imposition of a new obligation to immediately pay duty on goods brought to Australia under the current regime fails to meet this threshold in at least two major respects. First, leakage of arrived product from warehouses is not the primary source of illicit tobacco. Second, imposing this financial and administrative burden on all duty payers, in the absence of the identification of any specific duty evasion risk, is unprincipled and goes against the Government’s and ATO’s stated policies of only imposing regulatory burden on tax payers where specific risk is assessed to exist.

The rationale underpinning the new collecting tobacco duties and taxes at the border laws is to combat illicit tobacco.<sup>14</sup> The dominant source of illicit tobacco is not leakage from warehouses. Illicit importation is the largest source of illicit tobacco, by some orders of magnitude.<sup>15</sup>

<sup>12</sup> The Senate Select Committee on Red Tape, *Effect of red tape on tobacco retail, Interim report*, op. cit. at [2.63], available at [https://www.aph.gov.au/Parliamentary\\_Business/Committees/Senate/Red\\_Tape/Tobacco/Interim\\_Report](https://www.aph.gov.au/Parliamentary_Business/Committees/Senate/Red_Tape/Tobacco/Interim_Report).

<sup>13</sup> The Auditor-General, Australian National Audit Office, ANAO Audit Report No. 34 2015-2016, *Administration of Tobacco Excise Equivalent Goods – Australian Taxation Office and Department of Immigration and Border Protection*, op. cit. at [14 and Section 4], available at [https://www.anao.gov.au/sites/g/files/net4981/f/ANAO\\_Report\\_2015-2016\\_34.pdf](https://www.anao.gov.au/sites/g/files/net4981/f/ANAO_Report_2015-2016_34.pdf).

<sup>14</sup> *Excise Laws Amendment (Collecting Tobacco Duties at Manufacture) Bill 2018 and Excise Tariff Amendment (Collecting Tobacco Duties at Manufacture) Bill 2018, Explanatory Memorandum*; Department of Home Affairs Notice No. 2018/25, *Exposure draft of the Customs Amendment (Collecting Tobacco Duties at Manufacture) Bill 2018 for public consultation, Attachment A – Explanatory Materials*.

<sup>15</sup> The Parliament of the Commonwealth of Australia, House of Representatives, *Customs Tariff Amendment (Tobacco) Bill 2016, Explanatory Memorandum*, at [2.72]; Australian Taxation Office, *Inquiry into illicit tobacco, Parliamentary Joint Committee on Law Enforcement, ATO Submission*, at [8], available at [https://www.aph.gov.au/Parliamentary\\_Business/Committees/Joint/Law\\_Enforcement/Illicit\\_tobacco/Submissions](https://www.aph.gov.au/Parliamentary_Business/Committees/Joint/Law_Enforcement/Illicit_tobacco/Submissions); The Auditor-General, Australian National Audit Office, ANAO Audit Report No. 34 2015-2016, *Administration of Tobacco Excise Equivalent Goods – Australian Taxation Office and Department of Immigration and Border Protection*, op. cit. at [1.21], available at [https://www.anao.gov.au/sites/g/files/net4981/f/ANAO\\_Report\\_2015-2016\\_34.pdf](https://www.anao.gov.au/sites/g/files/net4981/f/ANAO_Report_2015-2016_34.pdf).

A Locked Mail Bag 1002  
Shellharbour City  
NSW 2529 Australia

9 Durgadin Drive,  
Albion Park Rail  
NSW 2527 Australia

T 1300 5655 2727

E [sales@tobaccoimportscompany.com.au](mailto:sales@tobaccoimportscompany.com.au)

The ATO's tobacco tax gap project has determined that for 2015-2016, the total tax gap arising from illicit tobacco was \$731 million, of which the vast majority of \$441 million is attributable to illicit importation channels (predominantly undeclared/misdeclared sea and air cargo), \$172 million is attributable to warehouse leakage and \$118 million is attributable to domestic 'chop chop' manufacture.<sup>16</sup>

**A** Locked Mail Bag 1002  
Shellharbour City  
NSW 2529 Australia  
9 Durgadin Drive,  
Albion Park Rail  
NSW 2527 Australia  
**T** 1300 5655 2727  
**E** sales@tobaccoimportscompany.com.au

To put the size and risk of the tax gap due to leakage from warehouses in context:

- the total net tax gap arising from all sources of illicit tobacco is 5.6% of the total tobacco market - which is a statistically significant, but not 'large' proportion; as the ATO has observed, "...previous illicit trade reports commissioned by the tobacco industry [and] the KPMG [2013 illicit tobacco] report...substantially exaggerate the size of the illicit tobacco market in Australia and the consequent loss of excise and duty revenue"<sup>17</sup>
- the tax gap arising from illicit (undeclared/misdeclared) importation accounts for over 60% of the total tax gap from illicit tobacco – it is the largest risk and source of illicit tobacco, by some orders of magnitude
- the tax gap arising from warehouse leakage accounts for 23.5% of the total tax gap from illicit tobacco
- illicit importation is the prime risk and source of illicit tobacco, accounting for substantially more than double the loss of revenue than warehouse leakage
- the estimated leakage from warehouses "represents less than 2% of warehouse throughput".<sup>18</sup>

The reasons that warehouse leakage is responsible for contributing substantially less to the illicit tobacco trade than illicit importation include that warehoused goods are subject to strict security, movement, compliance reporting, inspection and audit controls administered by the ATO.<sup>19</sup>

More generally, it has been acknowledged that "Australia has a strong legislative and regulatory framework to control illicit trade in tobacco products. The maximum penalty for tobacco smuggling, including conveying or possessing smuggled tobacco products, is now 10 years imprisonment in addition to pecuniary penalties of up to five times the amount of the duty evaded".<sup>20</sup>

Further and in relation to the contribution of warehouse leakage to the illicit tobacco trade, it appears that the conduct of the agencies responsible for administering warehouse controls has contributed to past occurrence of leaks by less-scrupulous warehouse operators and importers. An independent audit into the administration of tobacco excise equivalent goods conducted by the

<sup>16</sup> ATO tobacco tax gap report, available at <https://www.ato.gov.au/About-ATO/Research-and-statistics/In-detail/Tax-gap/Tobacco-tax-gap/>.

<sup>17</sup> The Parliament of the Commonwealth of Australia, House of Representatives, *Customs Tariff Amendment (Tobacco) Bill 2014, Explanatory Memorandum* at [2.105].

<sup>18</sup> ATO tobacco tax gap report, op. cit. available at <https://www.ato.gov.au/About-ATO/Research-and-statistics/In-detail/Tax-gap/Tobacco-tax-gap/>.

<sup>19</sup> Australian Taxation Office, *Submission – Inquiry into the effect of red tape on tobacco retail*, op. cit. at [15 and 18], available at [https://www.aph.gov.au/Parliamentary\\_Business/Committees/Senate/Red\\_Tape/Tobacco/Submissions](https://www.aph.gov.au/Parliamentary_Business/Committees/Senate/Red_Tape/Tobacco/Submissions); ATO tobacco tax gap report, op. cit. available at <https://www.ato.gov.au/About-ATO/Research-and-statistics/In-detail/Tax-gap/Tobacco-tax-gap/>.

<sup>20</sup> The Parliament of the Commonwealth of Australia, House of Representatives, *Customs Tariff Amendment (Tobacco) Bill 2014, Explanatory Memorandum* at [2.102]; The Parliament of the Commonwealth of Australia, House of Representatives, *Customs Tariff Amendment (Tobacco) Bill 2016, Explanatory Memorandum* at [2.70].



Australian National Audit Office concluded that “the administration [by the ATO and the predecessor to the Department of Home Affairs] of tobacco excise equivalent goods and the collection of customs duty has fallen short of effective practice”, as demonstrated by the fact that “reconciliation of the movement of underbond tobacco with the revenue collected or reported is seldom done...[and this] contributed to a lack of visibility and assurance around tobacco storage”.<sup>21</sup> The imposition of these burdensome measures onto business could be seen as an example of government asking business to pay for problems to which government agency administration and practices (or a lack of proper administration and practices) caused or contributed.

**A** Locked Mail Bag 1002  
Shellharbour City  
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9 Durgadin Drive,  
Albion Park Rail  
NSW 2527 Australia  
**T** 1300 5655 2727  
**E** sales@tobaccoimportscompany.com.au

We also note that the proposed collection of duty at the border measures are not expressly anticipated as being required for international best practice. Neither the WHO Framework Convention on Tobacco Control<sup>22</sup> (WHO FCTC) (to which Australia is a party) or the Protocol<sup>23</sup> currently under consideration expressly require or recommend the collection of duty at the border measures currently being considered. In respect of the control of duty-delayed warehouse goods, the WHO FCTC requires each State party to “adopt and implement measures to monitor, document and control the storage and distribution of tobacco products held or moving under suspension of taxes or duties within its jurisdiction”.<sup>24</sup> That is, these measures go beyond internationally accepted best practice.

Finally, the blanket imposition of this substantial financial impost on all importers, in the absence of the identification of any specific duty evasion risk, is unprincipled. An analogous area is the imposition of customs and excise quotas on tobacco manufacturers and importers, which the ATO acknowledges are only appropriately imposed “if a specific risk to revenue [in respect of individual duty payers] is identified...”.<sup>25</sup> The same can be said in relation to any requirement for duty payers to provide up-front and enduring security for any payment plan, again, in the absence of any specific identified payment risk or duty avoidance behaviour.

In effect, the imposition of these measures on duty holders who have bought goods to Australia in compliance with all laws and who have not demonstrated prior duty avoidance behaviour goes further than protecting revenue and penalises these businesses. It should also be remembered that the duty debt that will instantly arise on 1 July 2018 in respect of existing warehoused goods is not the result of non-payment of duty in the ordinary course or any non-declaration or misdeclaration by these importers, but is the peculiar or out-of-the-ordinary result of these changes in law, which represent a profound shift in the administration and regulation of tobacco import duty payments.

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<sup>21</sup> The Auditor-General, Australian National Audit Office, ANAO Audit Report No. 34 2015-2016, *Administration of Tobacco Excise Equivalent Goods – Australian Taxation Office and Department of Immigration and Border Protection*, op. cit. at [6 and 7], available at [https://www.anao.gov.au/sites/g/files/net4981/f/ANAO\\_Report\\_2015-2016\\_34.pdf](https://www.anao.gov.au/sites/g/files/net4981/f/ANAO_Report_2015-2016_34.pdf).

<sup>22</sup> World Health Organisation, *Framework Convention on Tobacco Control*, available at <http://apps.who.int/iris/bitstream/handle/10665/42811/9241591013.pdf?sequence=1>.

<sup>23</sup> World Health Organisation, *Protocol to eliminate illicit trade in tobacco products*, available at [http://apps.who.int/iris/bitstream/handle/10665/80873/9789241505246\\_eng.pdf;jsessionid=8BAF1C0C7B64067D316F7D16FA7DD36F?sequence=1](http://apps.who.int/iris/bitstream/handle/10665/80873/9789241505246_eng.pdf;jsessionid=8BAF1C0C7B64067D316F7D16FA7DD36F?sequence=1).

<sup>24</sup> World Health Organisation, *Framework Convention on Tobacco Control*, op. cit. at Article 15(4)(d).

<sup>25</sup> Australian Taxation Office, *Submission – Inquiry into the effect of red tape on tobacco retail*, 2017, at [37] and also see [20], available at [https://www.aph.gov.au/Parliamentary\\_Business/Committees/Senate/Red\\_Tape/Tobacco/Submissions](https://www.aph.gov.au/Parliamentary_Business/Committees/Senate/Red_Tape/Tobacco/Submissions); and also see Australian Taxation Office, *Practice Statement Law Administration 2012/3 ‘Determining and applying quotas under the Excise Act 1901’* at [1 and 7], available at <https://www.ato.gov.au/law/view/document?docid=PSR/PS20123/NAT/ATO/00001>.



Ordinarily when new laws are introduced, business interests are preserved through the grant of proper transitional arrangements, which effectively provide for the preservation of the status quo

for any business conducted prior to new laws coming into effect. In the absence of some particular risk considerations (which we submit do not arise in the present circumstances), that position should be adopted in relation to the new collection of duty at the border laws.

For any particular importers identified as having breached the duty laws and/or in respect of which a particular risk of duty avoidance or illicit diversion of goods is identified, the relevant agencies already have existing and more than sufficient investigation and enforcement powers, including the use of audits, imposition of licence conditions, seizure and destruction of goods, revocation of permission to enter goods and the imposition of penalties and imprisonment.

In the circumstances considered in this section of this submission, we submit that the imposition and/or effect of the requirement immediately to pay duty and treatment of existing warehoused goods as at 1 July 2018 do not meet the acknowledged thresholds for such imposition, either:

- Generally, given that the total net tobacco tax gap is 5.6% of the total tobacco market - which is a statistically significant, but not 'large' proportion
- In relation to warehoused tobacco, given that warehouse leakage is estimated to be responsible for far less of the total trade in illicit tobacco than the predominant source of risk, tobacco warehousing is already subject to strict controls which are policed by the ATO and the estimated leakage from warehouses represents less than 2% of warehouse throughput
- Specifically, in that these significant and financially burdensome measures are intended to be imposed on all importers, regardless of their prior clear duty payment compliance record and in the absence of any actual or reasonable basis to suspect that they may take steps to avoid the payment of duty.

## **5. The implementation of the new laws on duty-free goods gives rise to the same burden and risks to business as discussed above**

As TIC understands the position, the implementation of the new laws will require TIC immediately to pay duty on imported goods upon arrival in Australia for all goods, including those which will be sold through duty-free channels. We further understand that duty will not be included in the price paid by duty-free customers to tobacco importers. Rather, upon sale, the tobacco importer must claim a refund of the duty, similar to the existing duty drawback regime.

A description of the existing duty drawback scheme that has been accepted by the Red Tape Committee is that it is *"a specific area of red tape involving a 'complex, burdensome and redundant' process that incurs unnecessary business costs"*.<sup>26</sup>

As discussed above, the implementation of this aspect of the new laws will mean that importers are forced to fund the advance payment of duty, before being required to incur the administrative burden and delays associated with seeking a refund. This process amounts to unnecessary double-

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<sup>26</sup> The Senate Select Committee on Red Tape, *Effect of red tape on tobacco retail, Interim report*, June 2017, at [2.35], available at [https://www.aph.gov.au/Parliamentary\\_Business/Committees/Senate/Red\\_Tape/Tobacco/Interim\\_Report](https://www.aph.gov.au/Parliamentary_Business/Committees/Senate/Red_Tape/Tobacco/Interim_Report).

A Locked Mail Bag 1002

Shellharbour City  
NSW 2529 Australia

9 Durgadin Drive,  
Albion Park Rail  
NSW 2527 Australia

T 1300 5655 2727

E [sales@tobaccoimportscompany.com.au](mailto:sales@tobaccoimportscompany.com.au)

handling of duty. Unfortunately, it is not only the administrative costs which impact business – businesses will have to fund and finance the advance payment of duty, at substantial cost. Further, where the importers are in any event going to be entitled to a refund of the duty, this substantial cost is entirely unnecessary and only productive of wasted expenditure and financial strain on business.

The implementation of the new laws on duty-free goods suffers from the same burdens and risks as duty generally, including additional and unnecessary administrative red tape and financial burden, particular and unequal financial impact on small and medium businesses and a lack of a proper risk foundation.

## Conclusion

In order to avoid the inequitable and potentially market-distorting financial hardships described in this submission, small and medium businesses should be exempt from the new requirements.

Alternatively, small and medium businesses should automatically be granted payment plan terms, which should be exempt from interest and any requirement to provide security for those payment plans.

Alternatively, proper transitional arrangements should be put in place to preserve the status quo and not penalise businesses for engaging in current proper and lawful conduct. For existing warehouse stock, the effective date of the new laws should be deferred for 12 months, to 1 July 2020, to allow the orderly reduction of underbond stock in the usual course of business.

Without these measures, the new laws will dramatically and detrimentally affect the small and medium businesses which, together and separately, form a vital competitive counterpoint to the three large international businesses which comprise the remaining 98% to 99% of the Australian cigarette import market.

Regards

**Peter Rostirolla**  
Chief Financial Officer

**A** Locked Mail Bag 1002

Shellharbour City  
NSW 2529 Australia

9 Durgadin Drive,  
Albion Park Rail  
NSW 2527 Australia

**T** 1300 5655 2727

**E** [sales@tobaccoimportscompany.com.au](mailto:sales@tobaccoimportscompany.com.au)