



HM Revenue
& Customs



Border Force

Tackling illicit tobacco: From leaf to light

The HMRC and Border Force strategy
to tackle tobacco smuggling

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Foreword



Priti Patel

Exchequer Secretary
to the Treasury



James Brokenshire

Immigration Minister

Tobacco Excise Fraud is a crime which deprives the UK of vital revenue which could be used to fund essential public services, including tackling the damaging impacts of tobacco itself, but its impact extends far beyond that.

Dominated globally by organised criminals, the illicit trade damages legitimate business, undermines public health and facilitates the supply of tobacco to young people. The criminality involved, including the use of the proceeds to fund other crimes, has a devastating effect on individuals and communities across the UK and abroad.

Since 2000, when Her Majesty's Customs & Excise introduced its first strategy to tackle illicit tobacco, the progress in the fight against tobacco smuggling has been considerable. The size of the illicit cigarettes market has been halved and the illicit market for hand-rolling tobacco has reduced by a third. More than 26 billion cigarettes and 4,300 tonnes of hand-rolling tobacco have been seized. There have been more than 4,000 criminal prosecutions for tobacco offences. We have achieved a lot, but even this reduced illicit market still costs the taxpayer over £2 billion a year in lost revenues.

This strategy sets out not only how HMRC and UK Border Force will continue to target, catch and punish those in the illicit tobacco trade, but also how we will create an environment that is hostile to the fraud, from the streets of our cities where illegal tobacco products are sold to the factories across the world where those products start their journeys.

Working together is key to this approach, making sure that what we do to protect revenues complements our efforts to protect public health, the competitiveness of UK businesses, intellectual property, and the integrity and security of our communities. We are pleased to announce that HM Treasury will be establishing and leading a new ministerial group to champion cooperation between the many UK government departments and agencies who have a role to play in fighting this fraud, and to lead the effort to establish a shared understanding across the world of the damage it does.

A stylized handwritten signature of Priti Patel in black ink.

Priti Patel

A handwritten signature of James Brokenshire in black ink, written in a cursive style.

James Brokenshire

Executive summary

In 2013-14 HMRC collected £9.5 billion in tobacco duty, helping to fund vital government services.

In 2000, the illicit market shares were 22 per cent for cigarettes and 61 per cent for hand-rolling tobacco

In 2013-14, the illicit market shares were 10 per cent for cigarettes and 39 per cent for hand-rolling tobacco

The impact of tobacco smuggling

Tobacco smuggling costs over £2 billion in lost revenue each year. It undermines legitimate business and is dominated by internationally organised criminal groups often involved in other crimes such as drug smuggling and people trafficking.

The Government continues to take action to reduce smoking and the harm it causes. High duty rates, making tobacco less affordable, have helped reduce smoking prevalence in the UK from 26 per cent to 19 per cent over the last fifteen years. Tobacco smuggling undermines this, offering a cheaper way for those who might otherwise be deterred by cost to continue their habit.

What is tobacco smuggling?

All tobacco products sold in the UK are subject to excise duty. Any cigarettes or hand-rolling tobacco sold without this duty paid are illegal. While we continuously monitor the position, diversion from legitimate supply chains in the UK has not been an issue.

The problem is smuggling:

- Familiar UK brands, bought in other countries and smuggled.
- Overseas brands, smuggled and illegally sold in the UK.
- Unregulated products manufactured overseas and smuggled.
- Counterfeit products, sometimes manufactured in the UK from smuggled tobacco.

The illicit market has evolved. For cigarettes, we continue to seize significant quantities of UK and international brands and counterfeit product. However, the majority of illicit cigarettes targeted on the UK are unregulated products manufactured overseas. For hand-rolling tobacco, the illicit market is evenly split between UK and non-UK brands and counterfeit product.

How big is the problem?

In 2000, when the illicit market share for cigarettes was 22 per cent and 61 per cent for hand-rolling tobacco, Her Majesty's Customs & Excise introduced a strategy to tackle the problem. The problem remains significant. In 2013-14, the illicit market shares were 10 per cent for cigarettes and 39 per cent for hand-rolling tobacco.

How we are tackling tobacco smuggling

In April 2011, HMRC and Border Force jointly published the strategy ('Tackling Tobacco Smuggling – Building on Our Success'), to support sustained effort through to April 2015. We have reviewed this strategy to address changes in tobacco fraud.

Our aims are to:

- Create a hostile global environment for tobacco fraud through intelligence sharing and policy change.
- Tackle the fraud at all points in the supply chain from production to retail.
- Change perceptions - Raising public awareness of the links between illicit tobacco and organised criminality to reduce tolerance of the fraud in the UK.
- Optimise the use of the sanctions we have and, where we need to, develop tougher ones.

To do this we will:

Promote a UK and international agenda that will protect our policies and procedures from criminal attack, to stop fraud before it can take place.

Prevent fraud by using and developing regulatory frameworks.

Respond rigorously to attack those involved in the fraud, with interventions tailored to maximise the impact on them.

Section 1. A progress update

Since the launch of the Tackling Tobacco Smuggling strategy in 2000 we have had a significant impact in reducing the illicit trade. We have reduced the illicit market for cigarettes from 22 per cent in 2000-01 to 10 per cent in 2013-14 and for hand-rolling tobacco from 61 per cent to 39 per cent over the same period. Revenue losses have reduced from £3.4bn to £2.1bn a year over the lifetime of the strategy.

Revenue losses
have reduced
from £3.4bn
to £2.1bn a year
since 2000

Organised crime groups quickly respond to the controls introduced and new sources and types of illicit product emerge regularly. Key to the success of the strategic approach since 2000 has been the refresh of our strategy and re-assessment of the risks and emerging threats.

Our strategic approach has included regulatory change, new sanctions and detection technology and enhanced partnership working with other enforcement agencies, Department of Health, organisations such as Action against Smoking and Health and the tobacco manufacturers.

Tackling the threat presented by the criminality behind the fraud requires continuing collaboration across government in the UK and internationally.

We work closely with UK law enforcement agencies, such as Trading Standards, the police and licensing authorities, sharing and developing intelligence to support joint activity in the UK.

The UK continues to play a lead role in fostering international co-operation through our Fiscal Crime Liaison Officer (FCLO) network, international partnerships and playing a leading role in international programmes.

The UK has also championed international initiatives, such as the WHO Framework Convention on Tobacco Control, designed to reduce tobacco related deaths and disease, and the related Illicit Trade Protocol aimed at making further inroads into the global trade in illicit tobacco.

The 2011 strategy refresh led to

- Reduction of minimum Indicative limits for travellers from the EU.
- Agreement of a closer-working protocol with Trading Standards.
- Establishment of an Anti-illicit Joint Working Group with the tobacco manufacturers and work to use a new industry authentication system to tackle the illicit market.
- £25m investment provided through the 2010 Spending review for additional criminal investigators, expansion of overseas FCLO enforcement and intelligence activity and to strengthen border control of postal traffic.
- New technology to support detection and seizure of illicit tobacco coming via postal routes.
- A tougher approach on sanctions, with new sanctions following detection of illicit tobacco, and on supply chain enforcement.

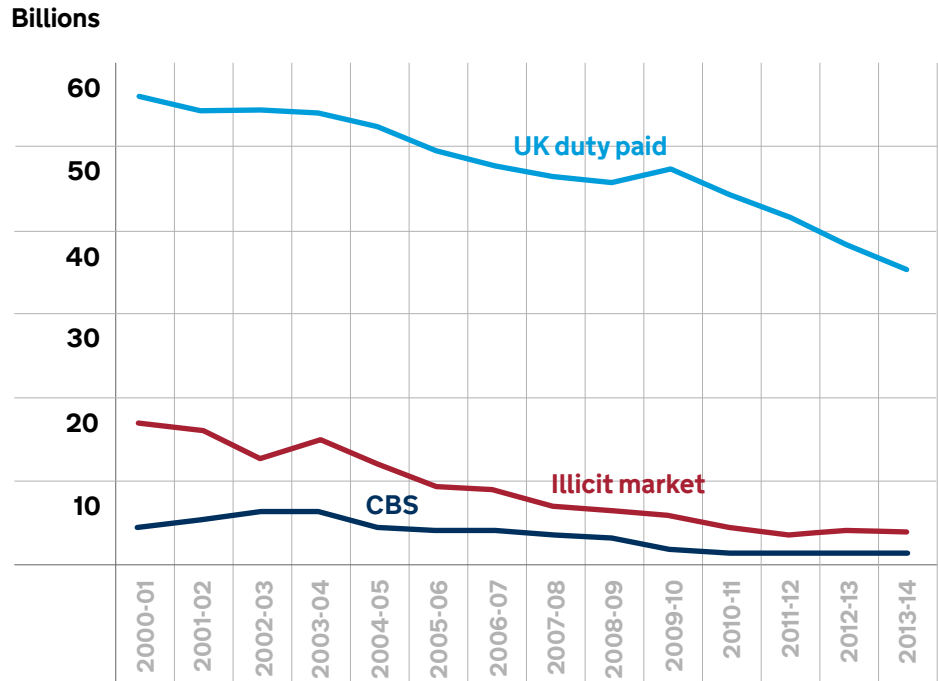
Our successes since the 2011 launch of the joint HMRC/Border Force strategy to tackle tobacco smuggling

| | |
|---------------|-----------------------------------------------------------------------------------------------------------------|
| £37.5 billion | Tobacco duty collected from April 2011 to end February 2015. |
| 6.4 billion | Non UK-duty paid cigarettes seized by HMRC and Border Force. |
| 1,621 tonnes | Non UK-duty paid hand-rolling tobacco seized by HMRC and Border Force. |
| 177 | People convicted of organised tobacco crime offences. |
| 605 | People convicted of smaller scale tobacco crime offences. |
| 50% | Increase in annual prosecutions for tobacco offences. |
| 3,300 | Assessments to recover unpaid excise duty. |
| 3,000 | Penalties issued for less serious tobacco offences. |
| £49 million | Value of penalties and assessments raised. |
| 200% | Percentage of duty evaded that can be charged as a penalty and assessment when illicit product has been seized. |

Estimated volumes of cigarettes consumed in the UK – UK duty paid, illicit and legitimate cross-border shopping (CBS)

Figure 1

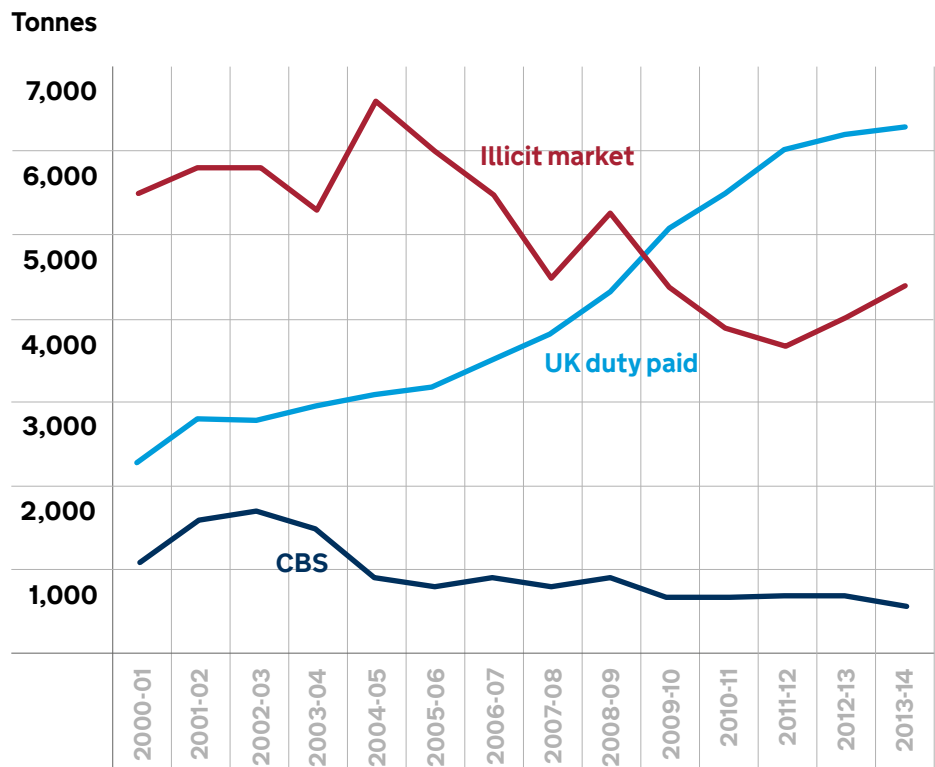
Cigarette sticks



Estimated volumes of hand-rolling tobacco consumed in the UK – UK duty paid, illicit and legitimate cross-border shopping

Figure 2

Hand-rolling tobacco



Tackling illicit tobacco: From leaf to light – case studies

A joint operation with our European partners prevented the loss of £250 million tobacco revenue and disrupted the activities of a major organised crime group

Overseas: International collaboration

In 2014 HMRC's Fiscal Crime Liaison Officer (FCLO) network identified a major illegal cigarette production network operating across several European countries and targeting the UK market. In July 2014, officers from Poland's Central Bureau of Investigation service, acting on FCLO intelligence, raided two premises near Krakow and seized 104 tonnes of processed tobacco, three cigarette production machines and two cigarette packaging machines. Six Polish nationals were arrested for excise evasion.

Following the successful raid in Poland, officers of the National Tax and Customs Administration of Hungary searched two connected premises on the outskirts of Budapest, seizing more than 36 tonnes of fine cut tobacco and 64,000 counterfeit 'Regal' brand cigarette cartons (sufficient to package 12.8 million cigarettes). This joint operation with our European partners prevented the loss of £250 million tobacco revenue and disrupted the activities of a major organised crime group.

At the border: The value of joint HMRC and Border Force intelligence activity

In December 2014, following the efforts of the joint HMRC and Border Force (BF) intelligence team, BF Officers at the port of Dover seized 6 tonnes of hand-rolling tobacco from RoRo (roll on/roll off vessel). HMRC circulated an immediate alert to other UK ports, notifying border teams of the type of consignments to profile, resulting in the seizure of a further 9 tonnes of hand-rolling tobacco, this time at a different port.

Using our network of contacts with worldwide law enforcement organisations HMRC collaborated with EU partners, who subsequently seized over 18 tonnes of hand-rolling tobacco relating to the same organised criminal group. An international operation is now being developed into the activities of the organised crime group behind the smuggling attempts.

At home: Working across government

More than one million suspected illicit cigarettes were seized during an operation to disrupt the sale and supply of illegal tobacco in Birmingham and Smethwick.

In January 2015, Officers from HM Revenue & Customs, supported by Birmingham City Council's Trading Standards team and Border Force, visited 22 retail premises and 17 self-storage units during an operation to disrupt the sale and supply of illegal tobacco in Birmingham and Smethwick.

The visits led to the seizure of more than one million cigarettes, including 632,000 from a self-storage unit in Birmingham and 297,000 cigarettes from a storage facility in Wednesbury. Cash totalling £12,000 and 23 kilos of tobacco were also seized from locations across the area. Had they reached the illicit market, the revenue lost to the UK exchequer would have been £260,000.

Section 2. Tackling illicit tobacco: From leaf to light

As criminals continue to exploit new opportunities to profit from the fraud, so our strategy must be dynamic and enable us to respond to new threats

Our ambition

In the longer term, we will work with partners in the UK and internationally to relentlessly pursue those behind the illicit market and change the perceived balance of risk and reward to eliminate the fraud.

In the medium term, our objective is to:

- Hold the cigarettes illicit market share at or below 10 per cent.
- Contain the illicit market share for hand-rolling tobacco and reverse the recent upward trend.

We will do this by:

- Continuing to do what we do well, retaining our focus on tackling organised criminal activity and high levels of seizures. We will strengthen our approach through improved targeting and prioritisation.

New approaches designed to:

- Create a hostile global environment for tobacco fraud.
- Reduce tolerance of the fraud in the UK.
- Improve coordination with partners in the UK and internationally to tackle the fraud at all points in the supply chain from production to retail.
- Optimise the impact of the sanctions available across government and introduce new ones when needed.

A constantly evolving fraud

As criminals continue to exploit new opportunities to profit from the fraud, so our strategy must be dynamic and enable us to respond to new threats. In 2011 a strong focus of our strategy was on cigarettes. Figure 1 on page eight shows good progress on that. While we need to maintain that, Figure 2 shows the need for the stronger focus from 2015-16 on hand-rolling tobacco.

Other recent changes in tobacco smuggling

The global footprint of smuggling has changed, as criminals exploit emerging international and political factors.

Cheap, factory-produced cigarettes have become increasingly available for large-scale smuggling.

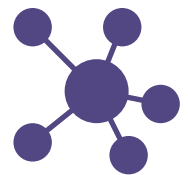
Smaller volume, higher frequency smuggling through non-traditional routes has increased.

Criminal sanctions currently have a limited long-term deterrent on 'career' fraudsters.

'Raw', unprocessed tobacco, presents an increasing duty-evasion risk. It is being used in the UK to illegally manufacture tobacco products subject to excise duty.

An evolving fraud requires a responsive strategy. We will track closely the impact we are having, refreshing aspects of the strategy if and when we need to, to ensure its effectiveness.

Alignment with HMRC's Compliance Strategy



Promote a wider understanding of the nature of the fraud at home and internationally, to maximise impact on its market and support mechanisms.

Optimise the use of regulatory frameworks to prevent the movement of illicit products along the supply chain.

Respond rigorously to detect, disrupt, punish and deter those involved in the fraud.

Promote

Sharing what we know to create a hostile global environment for tobacco fraud.
Reducing tolerance of the fraud in the UK through education and publicity.
Working together cross government to raise awareness.

Prevent

Strengthening controls on the movement of certain products e.g. raw tobacco.
Consulting on provisions in the WHO Framework Convention on Tobacco Control (FCTC), e.g. to register machinery used to manufacture tobacco.

Respond

Collaboration with UK and international partners to tackle fraud at all points in the supply chain.
Supporting EU ratification of the FCTC and introduction of the EU Track & Trace system and Security Feature in 2019.
Re-designing UK inland activity.
Extending use of sanctions available across government.
Identifying options to strengthen powers across government and their impact.

International engagement – Creating a hostile global environment for tobacco fraud through intelligence sharing and policy change

A change in the international approach to the fraud, to galvanise a sustained and coordinated attack on it across the world

The trade in illicit tobacco involves global supply chains, with the products crossing our borders being dependent on activity undertaken inside and outside the EU, controlled by organised networks of criminals and facilitated by many under their influence.

Achieving a shift in supply and demand for illicit tobacco needs a change in the international approach to the fraud, to galvanise a sustained and coordinated attack on it across the world.

The UK has been a leading player on the international stage in promoting awareness of the highly organised, global and serious criminal nature of the fraud and links with wider criminality, including leading the excise strand of the EU 'European Multi-disciplinary Platform Against Criminal Threats' (EMPACT) group, but more needs to be done.

With ministerial support we will step up our lobbying in Europe to highlight transit system abuse (T1), pressing for a step-change in the UK and international response to tobacco fraud, including stiffer sentencing, and raising awareness not only through Europol and OECD, but at G20 and G8

We will give strong and visible support to the new Latvian presidency of the EU in pressing for a clear timetable for the ratification of the WHO Framework Convention on Tobacco Control.

We will commission independent research, sponsored by ministers, into the global scale and impacts of the illicit tobacco trade from seed to smoke, using the outcomes to influence the international agenda at the highest level.

We will strengthen the impact of our Fiscal Crime Liaison Officer resource in key locations, improving intelligence flows between the UK and international partners and our global influence.

The work of the FCLO network resulted in seizures of over 1 billion cigarettes in each of the last three years

Supply chain – Undermining the profitability of the fraud at all points from production to retail

If unchecked, tobacco fraud can be highly profitable. Undermining that profitability requires sustained attack across distribution networks at all levels.

Effective exploitation of intelligence underpins our efforts and we have expanded the depth and breadth of our intelligence picture over recent years. This is supporting an ability to better identify, analyse and address new threats as well as to take action against the perpetrators of the crime, leading to higher numbers of criminal prosecutions.

We have achieved much. In particular, our FCLO network has proved a significant success in providing access to overseas intelligence on organised crime groups and their principals and a wider understanding of the underpinning criminal finances. The work of the network has also resulted in seizures of over 1 billion cigarettes in each of the last three years.

However, we can do more to:

- Increase our attack on organised crime groups.
- Optimise our use of intelligence to improve the impact of seizures.
- Reduce supplies of genuine products available for fraud.

We can do this through **regulation** and our enforcement **response**.

The Regulatory Framework

Smuggling does not seek to exploit loopholes, it simply evades and conceals. This limits the extent to which we can tackle it through regulatory controls, but we have used regulation successfully in the past and will continue to do so.

In 2006, we introduced legislation requiring the UK tobacco manufacturers to take steps to control the supply of product to high-risk markets from which smuggling is a problem. Since 2010, this has reduced supplies to these markets by 20 per cent for hand-rolling tobacco and 28 per cent for cigarettes.

For all controls we introduce, we continue to be mindful of the impact on legitimate business. Consultation ahead of increased regulatory control will be used to achieve the right balance to tackle threats proportionately.

The illicit market in hand-rolling tobacco, has reduced significantly since 2000, but the recent upward trend, from 35 per cent to 39 per cent in the last three years needs action. Following a consultation which closed on 30 January 2015, we plan to introduce controls for raw tobacco to mitigate the risk of it being used in the illicit production of smokeable product in the UK.

We will:

- Finalise proposals to introduce regulatory controls for raw tobacco to enable robust enforcement.
- Work with tobacco manufacturers to enhance supply chain control of UK product and to robustly challenge where appropriate.
- Consult on further controls within the WHO Framework Convention on Tobacco Control, including a potential licensing scheme for machinery to manufacture tobacco products.
- Support Department of Health, who will consult on the Tobacco Products Directive. A key component of this is a new EU wide Track & Trace system and Security Feature, so that genuine products can be tracked across the EU.

Our Enforcement response

The National Audit Office and Public Accounts Committee found that our current approach is logical and effective, but also made recommendations for improvement, including in our enforcement response. We have also taken into account changes in the UK illicit market in recent years. After a continuing downward trend in the illicit market since 2001-02, with market share for both cigarettes and HRT being at their lowest ever level in 2011-12, the last two years have seen increases. The tobacco tax gap in 2013-14 represents a revenue loss of £2.1billion so we need to continue our enforcement pressure, adapting where we need to in response to intelligence.

Sustaining our attack across the supply chain: What's new?

Targeting and disrupting Organised Crime Groups

- Increasing our focus on criminal finances: Taking the profit out of the crime and developing our understanding of the criminal finances behind the fraud. We will determine the structures used to fund fraudulent activity and use wide-ranging legal powers and partnerships with UK and global financial regulators and law enforcement bodies to mount a sustained attack on criminal finance networks.
- Extending offender management and the use of Serious Crime Prevention Orders: Stepping up the monitoring of the most serious offenders post sentencing to make it hard to participate further in the fraud.
- Increasing the impact of inland activity: Strengthening cross agency cooperation, including at ministerial level, building on our previous inland 'hot spot' programme and the sharing of intelligence between organisations and maximising co-ordination with other agencies across the distribution network to test risks and increase our UK intelligence coverage.
- Working with international partners to develop tactics to address the risk presented by overseas manufacturers.

Optimising the use of related intelligence to improve the impact of seizures

- Improving our use of intelligence to target interventions to maximise the impact of operational activity.
- Continuously improving joint HMRC/BF intelligence development: Enabling improved targeting of BF activity and a more flexible response, building on the development of existing joint intelligence teams and supporting effective joint operations.
- Disrupting the illicit production of hand-rolling tobacco in the UK by enforcing new controls on raw tobacco and taking action against organised crime groups responsible for its importation.

Consumers might not understand the extent of criminality, or how the profits they are contributing to may be used

Changing public perceptions – Reducing tolerance of the fraud in the UK

Outside those communities directly affected by the criminality behind tobacco fraud, there is a perception that it is a victimless activity. Even when consumers of illicit product suspect duty evasion has affected the price, they might not understand the extent of criminality beyond that, or how the profits they are contributing to may be used.

We will use behavioural insight to change attitudes, reduce tolerance of participation in the illicit market and raise public awareness of the criminality involved and the wider impact of the fraud.

We will:

- Work with other departments, agencies and organisations, including the tobacco manufacturers, Public Health England and Action on Smoking and Health and use additional communication channels available across these groups.
- Undertake targeted media and educational campaigns using behavioural levers to expose the true nature of the fraud and the consequences for those involved in it.
- Implement a new inland media strategy to ensure that messages are aligned with operational activity and tailored to resonate with local communities.

As part of this strategy, this year we will roll out a programme of educational campaigns, starting with hauliers, pub chains and self-storage facilities. These will use a variety of channels, including social media, available to HMRC and other public and private sector organisations, with continuing evaluation to develop our approach and maximise impact.

Getting tougher on those involved through Sanctions













HMRC, Border Force and other agencies have an extensive range of sanctions available to penalise those involved in the fraud. Our immediate priority is to ensure we use these effectively to maximise their impact.

We are developing a toolkit of sanctions for roll out in 2015, to ensure that officers consider all criminal and civil sanctions available to them to maximise impact and deterrent effect and will tighten policies where offenders are exploiting potential loopholes to avoid the full impact of sanctions. This will include ensuring cross-tax impacts are considered, to check the tax liabilities and benefit entitlement of offenders, and using those sanctions which agencies other than HMRC and Border Force may be able to deploy.

Border Force are also extending the use of immigration sanctions to refuse entry to the UK for tobacco smuggling where appropriate.

A fundamental review of sanctions

Current sanctions include:

-  Seizure of goods.
-  Seizure of vehicles/vessels.
-  Seizure of cash as the proceeds of crime.
-  Criminal prosecution with a custodial sentence of up to seven years.
-  Confiscation of assets as part of the proceeds of crime.
-  Assessment for the loss of duty.
-  Financial wrongdoing penalties of up to 100 per cent of the duty due.
-  Civil action, including winding up orders and bankruptcy.
-  Fines of up to £5,000 for selling illicit tobacco not bearing the UK duty-paid fiscal mark.
-  Prohibition on the sale of tobacco products for up to six months.
-  Referral for withdrawal of haulier's licence.
-  Naming & Shaming.

The sanctions available have developed piecemeal over many years. The time is right to take stock and assess whether tougher sanctions are needed, focusing across government on our objective of punishing and deterring criminal activity at all levels.

We will invite views from representatives of businesses affected by the fraud, local authorities, health groups and other law enforcement agencies through a consultation in 2015.

This will enable dialogue on a range of options across enforcement agencies, including the relationship between powers and existing regulatory requirements and joined up thinking across the tobacco control agenda, and will engage those affected by the fraud in considering how we might fundamentally change our approach.

