

**POST IMPLEMENTATION REVIEW:
DUTY FREE ALLOWANCES – CIGARETTES AND TOBACCO**

DEPARTMENT OF TREASURY

November 2015

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INTRODUCTION

The duty free allowances – cigarettes and tobacco measure (the measure) reduced the inbound duty-free allowance for cigarettes and tobacco from 250 cigarettes or 250 grams of tobacco to 50 cigarettes or 50 grams of other tobacco products, effective from 1 September 2012. The measure was announced in the 2012-13 Budget.

BACKGROUND

International travellers are able to bring into Australia limited quantities of certain goods free of duty. These can be purchased overseas or at duty-free stores located at international airports when arriving in Australia. Inbound duty-free stores are licensed to sell a limited range of duty-free goods such as alcohol, tobacco, perfume, photographic film, cosmetics and certain confectionery products.

Prior to the implementation of the measure, international travellers aged 18 years or over were allowed to bring up to 250 cigarettes (or 250 grams of other tobacco products) duty-free into Australia plus one open packet of cigarettes (up to 25 cigarettes).

PROBLEM

The 2012-13 Budget was framed around a fiscal strategy of returning the budget to a surplus. The budget was forecast to return to surplus in 2012-13, with surpluses growing over the forward estimates.

The economy was forecast to grow around trend, with low unemployment, contained inflation, record levels of mining investment and very low levels of government debt. Notwithstanding this, revenues continued to be affected by structural changes in the economy and the lingering effects of the global financial crisis—this led to weaker-than-expected tax receipts compared with those previously anticipated.

THE NEED FOR GOVERNMENT INTERVENTION

In response, the then Government decided on \$33.6 billion in targeted savings as part of a plan to return the budget to surplus. Revenue decisions accounted for just over half of those budget enhancing measures. The duty-free allowance measure was one of those revenue raising measures.

IMPACT ANALYSIS

REVENUE IMPACT

The measure was estimated to increase revenue by \$600 million from 2012-13 to 2015-16. This was intended to occur through incoming travellers substituting away from duty-free imported tobacco, in favour of purchasing tobacco products domestically where full excise is levied.

It is not possible to determine whether the \$600 million of additional excise revenue was ultimately achieved. This is due to two main factors:

- 1) A number of changes to tobacco policy have been made by governments in recent years, which would have also affected the tax rates and consumption of tobacco. There is insufficient information to disaggregate the impact of this single measure from the others.
- 2) The estimated increased revenue was expected to be collected from additional sales within Australia. Assessing this counterfactual is impossible as there is no information on what sales occurred within Australia as a result of reduced duty-free imports by travellers.

1) There were many changes to tobacco excise during the same period

Many changes to tobacco policies occurred around the same period of time as the measure. There is insufficient information to allow disaggregation of effects of the measure from the other changes to tobacco policies.

On 29 April 2010, the then Government increased the excise and excise-equivalent customs duty applying to tobacco products by 25 per cent, as part of a package of anti-smoking measures applying to tobacco products, including¹:

- a 25 per cent increase in excise;
- the introduction of the world's first tobacco plain packaging legislation;
- updated and expanded graphic health warnings on tobacco product packaging;
- extending restrictions on advertising to Australian internet advertising of products; and
- additional expenditure of \$27.8 million over four years on anti-smoking campaigns.

In the 2013-14 Budget, the then Government announced a four staged increase in tobacco excise and excise equivalent customs duty and swap from Consumer Price Index indexation to Average Weekly Ordinary Time Earnings (AWOTE) indexation.

The first three 12.5 per cent increases came into effect on 1 December 2013, 1 September 2014 and 1 September 2015. A further 12.5 per cent increase will occur on 1 September 2016. AWOTE indexation for tobacco excise and excise equivalent customs duty

¹ *Anti-Smoking Action*, joint media release from the Prime Minister, Treasurer and Health Minister, 29 April 2010.

commenced in 2014. Excise duty rates are indexed bi-annually on 1 March and 1 September each year.

2. Extra revenue not necessarily at the border

The estimated increased revenue attributed to the measure would not be collected solely at the border and there is no information on the individual transactions of travellers.

The original costing anticipated that there would be an aggregate increase in sales within Australia if travellers changed their behaviour to buy less duty-free tobacco prior to entering Australia and instead made a purchase at any tobacco retailer within the country.

Data on revenue collected at the border

Data on revenue collected at the border for Non-Commercial² tobacco importations by the Department of Immigration and Border Protection (DIBP) (then Australian Customs and Border Protection Service) shows an increase in customs duty paid after the measure took effect (see Table 4 below). It is possible that the higher revenues collected in years 2012-13 and 2013-14 from these declarations is partly attributable to the measure.

Change in behaviour at the border

As noted above, the original measure anticipated that the revenue would arise from domestic sales to travellers. In a subsequent decision, the Government allowed travellers the option, at the border of forfeiting tobacco which exceeds their allowance, or paying the appropriate rate of customs duty on the excess.³ This policy change would have reduced the effective cost of the duty-free limit changes to travellers and may have contributed to greater collections at the border.

Table 4: Customs duty collected from Non-Commercial tobacco importations (\$m*)

2009-10	2010-11	2011-12	2012-13	2013-14
2	1.5	1.5	4	4.5

*Rounded to the nearest \$500,000

Source: Department of Immigration and Border Protection

² Non-Commercial excludes importations reported through the Integrated Cargo System

³ 'Duty free allowances — amending the rules when incoming passengers declare and excess over the allowance' (p.161) in Commonwealth of Australia (2012), Mid-Year Economic and Fiscal Outlook 2013-14, 22 October.

OTHER IMPACTS OF THE MEASURE

Impact on duty-free stores

Possible impacts on duty-free stores could be⁴:

- A decline in tobacco sales due to the decreased duty-free inbound allowance for tobacco.
- Passengers deciding to purchase other duty-free goods in place of tobacco due to the duty-free allowance change. For example, a passenger may upon realising that there was a new allowance in place, could instead spend that money on another duty-free item such as alcohol which was not affected by the measure.

Travellers

Possible impacts on travellers could be⁵:

- Passengers that would have previously bought duty-free tobacco above the new allowance would have had their consumption choices restricted.
- Passengers that brought in tobacco above the new allowance would need to pay an upfront charge on their tobacco or forfeit that tobacco. This would impose an additional cost to those passengers upon entering Australia.
- Passengers that were above the new allowance who were unaware of the changes would have had to incur an unexpected upfront cost. This would impact their future spending.

REGULATORY BURDEN ANALYSIS

The regulatory cost of the measure is estimated to be approximately \$1.3 million per year over 10 years. This cost is expected to fall over time as most of the cost burden falls mostly on the first few years of implementation and then decreases over time as more people become aware of the reduced duty-free limit.

The regulatory cost of the measure arises from the cost imposed on international incoming travellers who were unaware of the new reduced duty-free tobacco limit and were carrying amounts of cigarettes or tobacco above the new limit (non-compliant travellers). Those non-compliant travellers would have been held up by Border Force officers upon entering the country and would have been required to either discard the excess tobacco or pay the amount on that tobacco.

⁴ These impacts are hypothecated. Actual impacts of the measure on duty-free stores were unable to be determined as they did not engage with Treasury's Post Implementation Review consultation process.

⁵ These impacts are hypothecated. Actual impacts of the measure on international travellers were unable to be determined as duty-free stores did not engage with Treasury's Post Implementation Review consultation process.

The regulatory costing used the following assumptions⁶:

- The daily rates of smoking from the NDSHS apply to all incoming international travellers.
- In the first year of implementation, 50 per cent of international travellers that brought in duty-free tobacco were non-compliant. The proportion of non-compliant travellers decreased by 25 per cent from the previous year each year.
- If there was no new reduced duty-free limit for tobacco, it is assumed that five per cent of international travellers who smoke would have been non-compliant⁷.
- The average amount of time that non-compliant travellers were held up by Border Force officers upon entering Australia was 10 minutes.
- The non-work related labour cost of \$27 per hour⁸ applies to non-compliant international travellers. This rate applies as international travellers are not working, they are traveling.

Other aspects of the assumptions are based on data on incoming international travellers from the Australian Bureau of Statistics website⁹ and data on the rates of daily smokers aged 18 years or older from the National Drug Strategy Household Survey (NDSHS)¹⁰.

DID THE POLICY RESULT IN A NET BENEFIT?

As mentioned previously, a number of other tobacco policy measures came into effect since implementation of the measure. It is not possible to isolate the impact of the measure due to insufficient information as outlined above.

However, for duty-free stores and international travellers, it is likely that duty-free stores experienced a decline in tobacco sales; in addition it is likely that some travellers would experience a decrease in their consumption choices and others would have had to pay an up-front cost at the border upon entering Australia.

⁶ No data exists concerning the actual amount of international travellers that were non-compliant with the measure or the average amount of time such travellers were detained by Border Force officials. The assumptions were developed for calculating an estimate regulatory burden for the purposes of the Post Implementation Review.

⁷ Data provided by the Department of Immigration and Border Force shows that non-compliant international travellers paid duty at the border under the previous duty-free limit (see table 4).

⁸ Non-work related labour cost rate provided by the Office of Best Practice Regulation Regulatory Burden Measurement Framework.

⁹ Australian Bureau of Statistics 2015, *Overseas Arrivals and Departures*, June 2015, cat. No. 3401.0, Australian Bureau of Statistics, Canberra

¹⁰ Australian Institute of Health and Welfare 2014. National Drug Strategy Household Survey detailed report 2013. Drug statistics series no. 28. Cat. No. PHE 183. Canberra: AIHW

It is not possible to draw a definitive conclusion on whether or not the measure resulted in a net benefit to the community.

IMPLEMENTATION AND EVALUATION

DIBP were responsible for implementation of the measure. After the measure was implemented, DIBP undertook an internal evaluation of its implementation of the policy. The evaluation concluded that the 2012 changes to the duty-free tobacco concession were implemented successfully. The changes were effected in a considered and timely fashion with minimal disturbance to relevant business as usual operations, and without major incident.

The communication delivered to international travellers of the changes via a public information awareness campaign was well developed, targeted and executed. Officers responsible for implementing the project were inventive in utilising mainstream communication channels as well as non-traditional, below-the-line channels, including the use of stakeholder communication channels, to disseminate notice of the changes.

The project was met with some hesitation from industry partners. However, considered and regular consultation took place and, where possible, co-designed solutions were explored. Pre-existing industry and government networks were well utilised in order to contribute to the solutions sought. Other government agencies, including border agencies, were consulted in a relatively minor capacity, but where consultation did take place outcomes were satisfactory.

The quantity of abandoned tobacco was far less than anticipated, in part because many travellers opted to pay the duty on excess tobacco rather than abandoning the goods.

There were a substantial number of passengers arriving in Australia that were unaware of the changes. There was a high level of in-store enquiries and uncertainty about tobacco allowances for both departures and arrivals in airports which suggested that communication with travellers could have been improved.

It was suggested that, in some cases, confusion relating to the duty-free concession had resulted in a rise in aggravated behaviour by passengers. However, the Australian Federal Police noted there was no substantial increase in incidents which required intervention by officers. It is likely this indicates that staff were well trained to deal with non-compliant travellers or that the awareness campaign was highly effective.

CONSULTATION

CONSULTATION IN RESPECT OF POLICY IMPLEMENTATION

DIBP were responsible for implementation of the policy. Stakeholders consulted as part of the implementation and the evaluation included:

- Border Force business areas including airport staff, communications and media, detained goods management and passengers policy and practice;
- airport operators;
- duty-free stores;
- peak industry bodies; and
- other government agencies.

DIBP consulted with the duty-free stores, airport operators and other interested organisations after the policy was announced.

Duty-free stores were broadly satisfied with the way DIBP implemented the measure. The duty-free stores felt they were kept fully informed about administrative issues and, when issues were raised, they felt that they were dealt with appropriately.

CONSULTATION IN RESPECT TO THE IMPACTS OF THE MEASURE ON DUTY-FREE STORES

Treasury attempted to consult with three duty-free stores, however, the duty-free stores did not engage with Treasury in the consultation process for the purpose of this review.

Phone calls were made and emails were sent on three occasions to the duty-free stores seeking to consult on the measure. The emails asked the following questions:

- Was there an impact to tobacco sales as a result of the duty-free measure? How significant was the change?
- Was there an impact to overall sales of duty-free goods or was there a shift to purchases of other duty-free goods?
- Did the measure have an impact on your stores' profits? If so, how significant was the impact?

The email also asked for any additional views on the measure that the stores may wish to express.