



TMA response to HMG's white paper on Customs

06th November 2017

The Tobacco Manufacturers' Association (TMA) is the trade association for the UK tobacco industry. The TMA's members are British American Tobacco UK Ltd., Imperial Tobacco Ltd. and Gallaher Ltd. (a member of the Japan Tobacco Group of companies).¹

The TMA welcomes the Government's invitation to comment on its white paper on future customs arrangements as the UK leaves the EU. It is vital to the industry that customs issues are settled well ahead of departure from the EU.

Failure to achieve fluid and un-bureaucratic customs processes would risk dramatically increasing business costs at the expense of investment in the UK and the jobs of thousands directly employed by the industry and tens of thousands in associated industries.

Moreover rising costs due to lack of suitable customs arrangements would undermine the public finances as smokers would likely be further pushed into the illicit and cross-border tobacco markets. This would add to the tobacco tax gap which is already worth £3.1 billion² and further undermine the £11.5 billion tax contribution made by the industry each year.

Summary response to HMG Customs white paper:

1. The TMA supports the aim of frictionless trade by introducing a highly streamlined customs arrangement rather than the option of a 'new customs partnership'.
2. The TMA agrees with the Government's proposals to simplify the movement of goods and increase capacity at the customs border.
3. The TMA agrees that there should be a time-limited transitional period.
4. The TMA does not agree that there should be no changes to personal import rules.
5. Planning for a contingency scenario is a sensible precaution but the government should make all efforts to avoid this course.

¹ <http://www.the-tma.org.uk/about/>

² HMRC, 2017, Measuring tax gaps, tobacco tax gap estimate 2016-17

Overall the TMA believes the Government is taking the correct approach towards customs issues. However, as will be detailed further, it is clear that much further work is needed to deliver the Government's aims and consequently there remain significant uncertainties.

To that end, the Government should commit to updating businesses on the progress of customs arrangement negotiations to allow them to plan accordingly. The Government should also make necessary funds available at the Budget to ensure that suitable arrangements are in place.

Discussion of the Issues

1. A highly streamlined customs border over a new customs partnership

The TMA's member companies support the proposal for a highly streamlined customs border. This does present risks to the easy flow of goods, but it would provide more certainty than the alternative option being considered.

The 'new customs partnership' scheme seems overly complex and as has been described by Open Europe as "too clever by half". This seems a fair reflection of the proposal as it would require the tracking of an enormous amount of products.

Illustrating this by way of an analogy, the tobacco industry is currently considering how to accommodate the European Commission's draft regulations requiring all economic operators to track and trace all tobacco products to the first customer level (as mandated in Articles 15 & 16 of the revised Tobacco Products Directive). These requirements go beyond what is required by the Directive, are very complicated, present a major logistical challenge and are expected to be very costly in their current form³.

Presuming these regulations are roughly similar to the requirements that would be placed on all importers and exporters in the 'new customs partnership' proposal, the TMA is of the opinion that it would be unfeasibly expensive and disruptive. Even supposing that the requirements in this new customs system were less onerous than the heavy handed ones imposed on the tobacco industry, it seems unlikely that they would be practicable on such a wide scale.

The need to introduce a rebate system where businesses have automatically had to pay the highest potential tariff on import of a good would disrupt business cash flows and adds a further unnecessary complication to the system beyond the technicalities of implementation.

The potential requirement of further legislation to deliver the 'new customs partnership' would also undermine business confidence as it would reduce the certainty of outcome for future customs arrangements and may take up parliamentary time which is required for other matters.

As the Government notes, the 'new customs partnership' proposal is "untested", it should remain so.

³ The TMA has detailed policy positions regarding Articles 15 & 16 available on request.

2. Achieving a highly streamlined customs border

Given the impracticalities of the 'new customs partnership' the Government should focus on achieving a highly streamlined EU customs border. This appears to have two main criteria: 1.) reducing the burden of administration and paperwork at the customs border; 2.) Ensuring there is sufficient capacity at the customs border to avoid delays (obviously, the success of the former will impact the importance of the latter).

Firstly, on minimising the administrative burden, the specific examples the Government gives in the white paper would be welcome.

- A continued waiver from the need to submit entry and exit summary declarations and remaining a member of the Common Transit convention would promote continuity.
- The Government should ensure that the UK's AEO scheme is recognised by EU states and should automatically register businesses which currently have AEO status (including TMA member companies) in any new scheme.
 - This is particularly important as loss of AEO status (even if only temporary) may require companies to seek costly guarantees from banks.
- A bilateral agreement to notify the relevant authorities of consignments ahead of arrival at Ro-Ro ports could ease the traffic flow.
- The ability to self-assess and aggregate payments of Excise Duty and VAT should be continued to avoid creating further cash-flow issues.

Secondly, whatever measures the Government takes to reduce the burden of customs formalities, due to the large increase in volume of declarations, the Government must also consider how to increase capacity physically, in terms of manpower and in its IT systems.

- Continuing to upgrade CHIEF to the new CDS in line with the Union Customs Code with much greater capacity is the right move, but given the tight timeframe it would be prudent to consider additionally upgrading the capacity of CHIEF as a fall back option should CDS not be available in full on time.
- Physical space is probably going to be even more problematic, and in conversations with other industries, the TMA has noted particular concern over space at Ro-Ro ports such as Dover. The Government should consider how to take the customs procedures away from the border to allow traffic that does not require checks to continue its passage.
- Without sufficient staffing to manage the additional customs procedures, the upgrades to physical and IT capacity may end up worthless. The Government must conduct an urgent review into the capacity and capabilities of the current customs workforce with regard to the large growth in customs procedure volumes they will experience. Following this, the Government should begin investing in additional staff and training immediately as required. It is encouraging that media reports indicate progress is being made in this regard⁴.

⁴ <http://www.independent.co.uk/news/uk/politics/brexit-latest-staff-numbers-new-hmrc-jobs-employ-david-davis-a8030281.html>

- The Government is looking to increase automation and this may reduce any manpower pressures through speedier processes but it would be unwise to make bold assumptions about this and it should be considered a longer-term prospect. Automation is, in the view of the TMA, unlikely to be a panacea for short term post-Brexit customs problems and it would be risky to rely on its success too heavily at an early stage of its development.

While there is much noted here that the Government can progress with, it remains unknown exactly what customs formalities will be required. These will impact on businesses as they may have to adjust staffing levels and processes to respond to changing challenges. This reinforces the need for clarity and advanced warning about additional requirements as noted in the summary response section.

3. A time-limited transitional period

The issues that will need to be negotiated and agreed may take longer than the Article 50 timetable allows. And the implementation and smoothing of any new systems may take additional time. Given this, an interim transition period is a sensible option and should be negotiated as a priority to give businesses confidence that they have sufficient time to respond to any new requirements. The TMA also agrees that this transitional period should be time-limited in order that there remains an incentive for both the UK and the EU to work towards a final customs agreement.

4. Changes to personal import limits

The TMA understands that, if the UK reverts to trading under WTO rules (as per the contingency scenario), we would temporarily be allowed to have different rules for personal tobacco imports from EU and non-EU countries (HMG notes this option in paragraph 5.42 of the White Paper). In due course the UK would have to apply the same rules to personal imports from all countries.

However, the TMA is of the opinion that the Government should immediately introduce fixed limits for personal tobacco imports from the EU regardless of the final outcome of the customs and trade negotiations. These could be in line with current Duty Free limits (e.g. 200 cigarettes or 250g RYO).

Currently there is no limit on personal tobacco imports for personal use. Officials use minimum indicative levels (MILs) as guidelines for quantities of tobacco products which may arouse suspicion (e.g. above 800 cigarettes) - although there is no free-pass below these levels. However, this lacks clarity and requires enforcement officials to make difficult judgements of the intentions of a passenger with a large amount of tobacco. Consequently there is abuse of the MILs.

Some individuals bring tobacco into the UK from other EU Member States, ostensibly for personal use, and sell it on without paying additional UK tobacco duty. The prevalence of such 'ant smuggling'⁵ as a method of bringing non-UK duty paid tobacco into the UK could be countered by introducing fixed limits.

⁵ As discussed in RUSI analysis in KPMG, 2017, Project SUN

TMA conversations with border enforcement officials suggests they would welcome the clarity that this would bring them, saving time and improving productivity when there are likely to be significant additional burdens placed on them.

The tax gap from illicit and cross border tobacco increased to £3.1 billion in 2016-17 from £3bn the previous year (HMRC) and it is expected that this could be reduced by introducing fixed limits. So while this policy may require additional enforcement, it is possible (and even likely) that in time the reduction in lost duty would mean the move would pay for itself and more.

5. Contingency scenario

Leaving the Customs Union without an agreement with the remaining EU member states (particularly over a transitional period) is to be avoided.

Customs delays and higher costs to business become significantly more likely if the Government has only 18 months to deliver new systems rather than a longer period of time. If the UK and the remaining EU nations did not achieve recognition of each other's' customs systems the disruption would be even greater as it is expected that paperwork would increase and procedures would lengthen.

The introduction of tariffs on tobacco products should also be avoided in the contingency scenario. Tariffs would push up tobacco prices exacerbating the illicit trade or, if compensatory measures were taken in the excise regime, it would add significant complexity to the system. In either case, this would risk reducing tobacco duty revenues.

Moreover there will be little to no domestic tobacco manufacturing to protect by 2019 and as the industry already contributes approximately £11.5 billion in tax each year further impositions cannot be justified⁶.

Conclusion and key recommendations

While the TMA believes the plan for a highly streamlined customs border is the right approach, ultimately its success will depend on effective and timely implementation of this plan. The TMA makes the following key recommendations:

- The Government should make customs a priority in negotiations with the EU, particularly with the aim of agreeing a transitional arrangement.
- The Government should make the customs requirements businesses will face in the future known at the earliest possible time.
- The Government should use the forthcoming budget to commit further resources for upgrades to capacity (physical, workforce and IT) at customs pinch points.

⁶ Further details on the TMA's positions on tariffs can be found on our website or by contacting the TMA.