



HM Revenue
& Customs

Measuring tax gaps 2017 edition

Tobacco tax gap estimates for 2016-17



Estimating tobacco tax gaps for 2016-17

- 1.1 This statistical release presents estimates of the tax gap for tobacco products in 2016-17. Estimates for years up to 2015-16 are published in 'Measuring tax gaps 2017'. Online tables which contain a full-time series of the tobacco estimates can be found on our website www.gov.uk/government/statistics/tobacco-tax-gap-estimates.

Tobacco

- 1.2 The tobacco tax gap is driven by the illicit markets in cigarettes and hand-rolling tobacco and was estimated to be £2.5 billion in 2016-17. Of this £1.9 billion was lost in tobacco duties and a further £0.6 billion in VAT.
- 1.3 In 2016-17 the cigarette tax gap was estimated to be £1.8 billion and the hand-rolling tobacco tax gap was estimated to be £0.7 billion. The central estimate should be interpreted as an indicator of long-term trends rather than a precise estimate of year-on-year changes.
- 1.4 Trends in the cigarette and hand-rolling tobacco market appear to be diverging. UK tax-paid consumption of cigarettes continues to fall whereas the UK tax-paid consumption of hand-rolling tobacco has steadily increased since 2005-06, levelling off in recent years. There may be a number of reasons for this difference, including consumer preference, price, and policy initiatives.
- 1.5 The central estimate for cigarette consumption decreased from 64 billion cigarettes in 2005-06 to 36.5 billion cigarettes in 2016-17. The central estimate of 36.5 billion cigarettes in 2016-17 should be interpreted in the context of statistical uncertainty, with an upper estimate of 38 billion cigarettes and a lower estimate of 34.5 billion cigarettes.
- 1.6 In 2016-17 the central estimate for hand-rolling tobacco consumption was 9,700 thousand kg (with an upper estimate of 10,300 thousand kg and a lower estimate of 9,000 thousand kg). The central estimate for hand-rolling tobacco consumption peaked in 2013-14 at 11,500 thousand kg and has been decreasing since.
- 1.7 The previously published estimates for 2014-15 and 2015-16 have been revised due to a revision in a cross-border shopping data source.
- 1.8 The combined tobacco tax gap is the sum of the central estimates for cigarettes and hand-rolling tobacco. It is not possible to combine both upper (or lower) estimates simultaneously, so there is no upper or lower bound estimate for the combined tobacco tax gap.
- 1.9 Further information on the upper and lower bounds is covered in the section on tobacco methodology and the data issues section below. You can find full details in the Methodological Annex that is published alongside 'Measuring tax gaps 2017' on our website www.gov.uk/government/statistics/measuring-tax-gaps

Table 1.1: Tobacco Tax Gap (£ million)^{1,2,3}

	2005-06	2010-11	2011-12	2012-13	2013-14	2014-15	2015-16	2016-17
Cigarette illicit market⁴								
Upper estimate	2,400	1,700	1,600	1,900	2,000	1,500	2,200	2,300
Central estimate	1,900	1,200	1,000	1,300	1,400	900	1,600	1,800
<i>of which VAT</i>	300	200	200	300	300	200	300	400
<i>of which duty</i>	1,500	900	800	1,000	1,100	700	1,300	1,400
Lower estimate	1,400	700	400	600	800	400	1,000	1,200
Hand rolling tobacco illicit market⁵								
Upper estimate	1,000	900	1,000	1,100	1,200	1,000	1,000	900
Central estimate	800	700	800	900	1,100	900	800	700
<i>of which VAT</i>	200	200	200	200	300	200	200	200
<i>of which duty</i>	700	500	600	700	800	700	600	500
Lower estimate	700	500	600	700	900	700	600	500
Combined tobacco illicit market⁶	2,700	1,900	1,800	2,200	2,500	1,800	2,400	2,500

1 Figures for previous years have been revised.

2 Figures are independently rounded to the nearest £100 million.

3 Includes both duty and VAT.

4 Based on the weighted average price (WAP) of all UK duty paid cigarettes.

5 Weighted average price (WAP) data for all UK duty paid hand rolling tobacco is not available prior to 2012-13, so the losses are based on the price of a 'typical brand'.

6 The upper (or lower) bounds for both cigarette and hand rolling tobacco cannot be combined. Only the central estimates are simultaneously possible.

Cigarettes

- 1.10 Total consumption is obtained from the Opinions and Lifestyle Survey conducted by the Office for National Statistics (ONS). The sample is representative of the cigarette-smoking population, but as with all surveys, it suffers from sampling error.
- 1.11 UK tax-paid cigarette consumption has declined steadily from 49.5 billion cigarettes in 2005-06 to 29.5 billion cigarettes in 2016-17.
- 1.12 There has been a long-term decline in the estimated volume of cigarettes in the illicit market from 2005-06, when the central estimate for the illicit market was ten billion cigarettes in the UK. Since 2010-11, the central estimate of the illicit market has been fairly stable, varying between three billion cigarettes and 5.5 billion cigarettes.
- 1.13 Previously, there had been a long-term decrease in the central estimate of the cigarette tax gap from 16% in 2005-06 to 8% in 2014-15. The central estimate rose in 2015-16 and 2016-17, driven by total cigarette consumption continuing to decline while the central illicit cigarette market remains fairly stable. However, throughout the time series, year-on-year changes have been inconsistent and the central estimate should be interpreted as an indicator of long-term trends rather than a precise estimate of year-on-year changes.

Table 1.2: Cigarettes: Illicit market share and breakdown of volumes (billion cigarettes)^{1,2}

	2005-06	2010-11	2011-12	2012-13	2013-14	2014-15	2015-16	2016-17
Illicit market share								
Upper estimate	19%	14%	13%	15%	15%	12%	17%	18%
Central estimate	16%	10%	8%	10%	11%	8%	13%	15%
Lower estimate	12%	6%	3%	5%	6%	4%	8%	11%
Total consumption								
Upper estimate	66.5	53.0	49.5	47.0	43.5	39.5	40.5	38.0
Central estimate	64.0	51.0	47.0	44.5	41.5	38.0	38.5	36.5
Lower estimate	61.5	49.0	44.5	42.5	39.5	36.0	36.5	34.5
UK tax paid consumption	49.5	44.5	41.5	38.5	35.5	33.5	32.0	29.5
Illicit market								
Upper estimate	12.5	7.5	6.5	7.0	6.5	5.0	7.0	7.0
Central estimate	10.0	5.0	4.0	4.5	4.5	3.0	5.0	5.5
Lower estimate	7.5	3.0	1.5	2.5	2.5	1.5	3.0	4.0
Cross-border shopping ³	4.0	1.5	1.5	1.5	1.5	1.5	1.5	1.5

1 Figures for previous years have been revised.

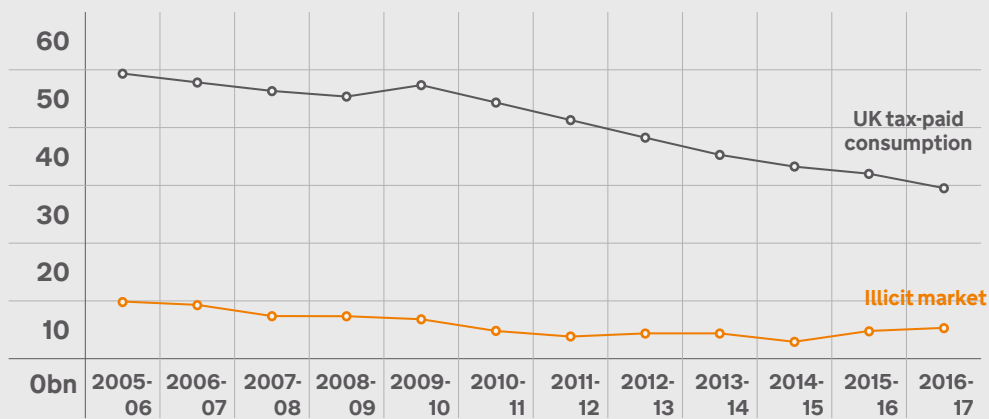
2 Figures are independently rounded to the nearest 1% or 0.5 billion cigarettes.

3 Includes duty-free as well as EU duty paid.



Tobacco tax gap estimates 2016-17 is available on our website
www.gov.uk/government/statistics/tobacco-tax-gap-estimates

Figure 1.1: Cigarette central estimate for illicit market and UK tax-paid consumption (billion cigarettes)



Hand-rolling tobacco

1.14 The tax gap for hand-rolling tobacco was estimated to be 28% in 2016-17. The long-term trend is of a relatively steady decrease in the tax gap, down from 60% in 2005-06. The central estimate should be interpreted as an indicator of long-term trends rather than a precise estimate of year-on-year changes.

1.15 The UK tax-paid consumption of hand-rolling tobacco increased steadily between 2005-06 and 2013-14 and has been relatively stable since then. The illicit market volume of hand-rolling tobacco has shown a long-term decline since 2005-06 and in 2016-17 was estimated to be 2,700 thousand kg.

Table 1.3: Hand-rolling tobacco: Illicit market share and breakdown of volumes (thousand kg)^{1,2}

	2005-06	2010-11	2011-12	2012-13	2013-14	2014-15	2015-16	2016-17
Illicit market share:								
Upper estimate	65%	46%	43%	43%	44%	39%	38%	33%
Central estimate	60%	39%	37%	37%	40%	35%	32%	28%
Lower estimate	55%	33%	31%	32%	36%	30%	27%	23%
Total consumption								
Upper estimate	11,200	11,400	11,400	12,100	12,300	11,200	10,700	10,300
Central estimate	10,200	10,400	10,600	11,200	11,500	10,500	9,900	9,700
Lower estimate	9,100	9,500	9,700	10,300	10,800	9,900	9,200	9,000
UK tax paid consumption	3,200	5,500	6,000	6,200	6,300	6,300	6,200	6,400
Illicit market								
Upper estimate	7,200	5,200	4,900	5,200	5,500	4,400	4,000	3,400
Central estimate	6,100	4,200	4,000	4,200	4,700	3,700	3,300	2,700
Lower estimate	5,000	3,200	3,100	3,300	3,800	3,000	2,500	2,100
Cross-border shopping ^{3,4}								
Associated with upper estimate	700	600	600	700	500	500	500	500
Associated with central estimate	800	700	700	700	600	600	500	500
Associated with lower estimate	900	800	700	800	600	600	500	500

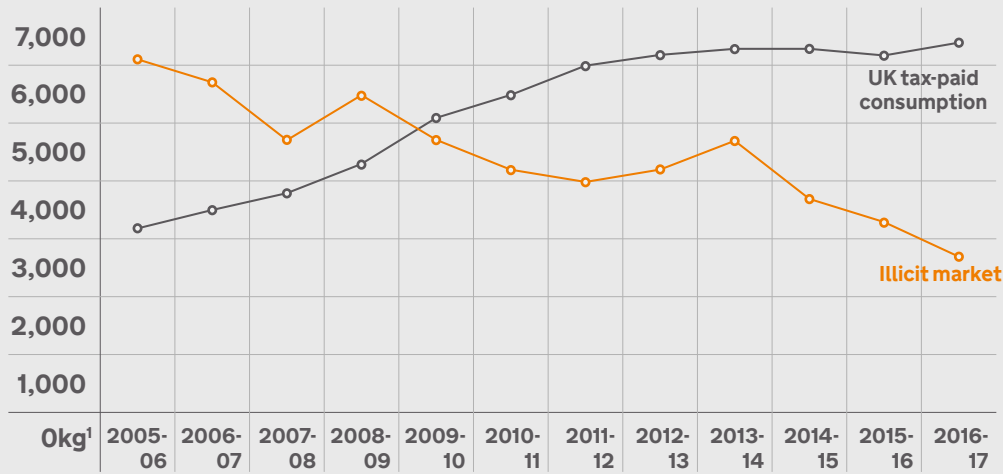
1 Figures for previous years have been revised.

2 Figures are independently rounded to the nearest 1% or 100,000kg.

3 Includes duty-free as well as EU duty paid.

4 Since January 2004, an improved data source has been used to estimate cross-border shopping, but cannot be applied to earlier years.

Figure 1.2: Hand-rolling tobacco central estimate for illicit market and UK tax-paid consumption (thousand kg)



1 Thousand kg

Tobacco methodology and data issues

- 1.16 The estimates are produced using a 'top-down' methodology: the total consumption is estimated, the legitimate consumption is subtracted, and the remainder is the illicit market.
- 1.17 Total consumption is estimated using data from the ONS Opinions and Lifestyle survey. Legitimate consumption is based on the returns HMRC receives from the volumes of tobacco on which duties have been paid and an estimate of cross-border shopping and duty-free sales.
- 1.18 In addition to the uplift that accounts for under-reporting, there is an uplift that accounts for people who falsely deny smoking, which comes from the Health Survey for England.
- 1.19 The estimates are presented within a range defined by the upper and lower estimates. The range provides an indication of the size of the illicit markets in cigarettes and hand-rolling tobacco, depending on how dual smoker survey respondents are treated.
- 1.20 The upper bound for cigarettes corresponds to a scenario where the majority of dual smokers consume cigarettes. The lower bound for cigarettes is calculated when the majority of dual smokers are assumed to smoke hand-rolling tobacco. The upper and lower estimates for hand-rolling tobacco are calculated in a similar way. This means that the upper (or lower) bounds for both cigarettes and hand-rolling tobacco cannot be possible at the same time.
- 1.21 The central estimate reported here should be interpreted as an indicator of long-term trends rather than a precise estimate of year-to-year changes. The range provides an indication of the size of potential systematic errors due to the use of survey data.



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