

Illicit Trade 2015-2016

Implications for the Irish economy

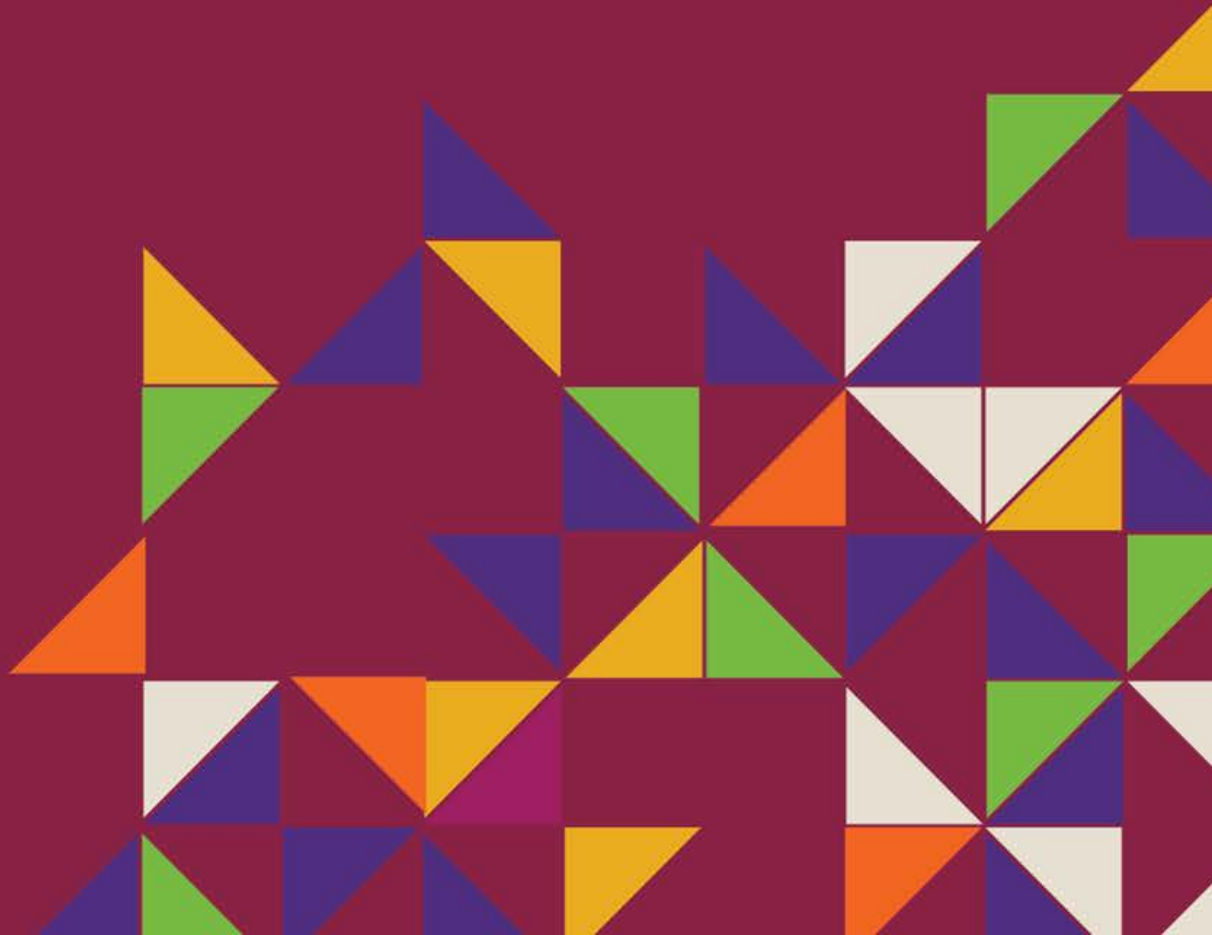


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Introduction



Introduction

Welcome to the third in our series of annual reports on **Illicit Trade in Ireland**. This report updates many of the issues and detail previously provided. Copies of previous reports are available on our website.

2013 report

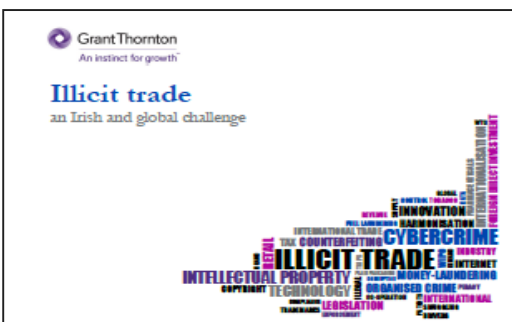


Our first report in 2013 entitled “Illicit Trade in Ireland – uncovering the cost to the Irish economy” focussed on a number of areas in the retail sector. This report was prepared in conjunction with Retail Ireland.

The highlight of the first report was a quantifiable estimate of the total cost of illicit trade to the economy across the fuel, tobacco, digital piracy and pharmaceutical sectors. The report outlined detailed analysis of the cost to right holders and the Exchequer. The total loss was quantified in the range of circa €600m to €1.5bn.

The report also highlighted the vital role that Intellectual Property (IP) plays in promoting innovation and stimulating the economy to foster growth. Despite the obvious importance of IP rights and the emphasis on the necessity to protect these rights, the report highlighted the deficiencies and challenges in which the key drivers of illicit trade impact on this activity. The report highlighted the recurrent theme of the clear linkage of organised crime across illicit activity and made recommendations on areas where improvement could be made.

2014 report



The second report in 2014 entitled “Illicit Trade – an Irish and global challenge” expanded on the analysis and findings of the 2013 report to include the impact and cost of cyber crime and money laundering. The analysis concluded that cyber crime is costing the Irish economy €630m annually and given that our fast-growing technology sector is a key economic driver, the importance of Ireland taking the lead on tackling this issue was underlined. The report discussed the proceeds of criminal activity, including the proceeds of illicit trade, which are converted to cash on some basis and laundered through the cash economy and financial institutions.

The report estimated that as much as €5.4 billion is laundered in Ireland but acknowledged that although Ireland has made significant progress in terms of legislative changes more improvements are required.

Regarding IP intensive industries, the report pointed out that Ireland has the largest contribution to Gross Domestic Product (GDP) of such industries in Europe. Notwithstanding protection and progress in developed economies the report pointed out that there is poor protection and incentive for improvement in less developed countries. The report called for increased collaboration with developed countries in the development of IP protection.

As regards the level of illicit activity in the retail sector, the 2014 report noted that the illicit activity showed little signs of abating and that the estimate of c€600m to €1.5bn total loss to the economy reported in 2013 was still the best estimate.

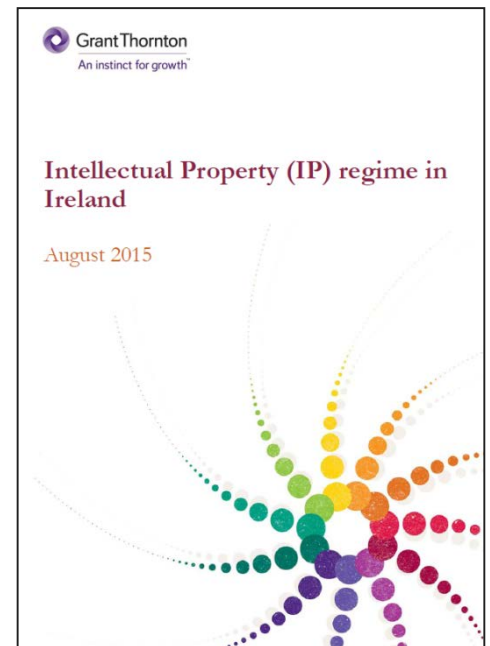
2015 reports

When the 2013 and 2014 reports were launched and published, they each attracted significant commentary in media and from interested stakeholders. Whilst some of the estimates, findings and commentary were questioned and sometimes disagreed with, we welcomed active feedback and discussion to ensure that the core issue of the protection of IP and the consequences of illicit trade for the economy, right holders and society were actively debated. Debate encourages action and change and in some sectors such as fuel laundering, positive changes are starting to have an impact. The report attracted the attention of the British-Ireland Parliamentary Assembly (BIPA) and Grant Thornton were invited to present the report to the Committee on Cross Border Police Cooperation. The parliamentarians were keen to see a widening of future reports to deal with aspects of the border/all island economy. This updated report deals with these issues in greater detail.

In August 2015, we published a report entitled "Intellectual Property (IP) regime in Ireland" which outlined the different types of IP, the legislative framework and key developments which will impact on the holders of IP. The most significant IP development over the past year has been the enactment of legislation to enable the introduction of plain packaging on tobacco products. Notwithstanding the impact on tobacco products and the potential increase in illicit activity in this sector, there are concerns from other sectors and stakeholders/commentators on IP about the containment impact further legislative hinges could bring.

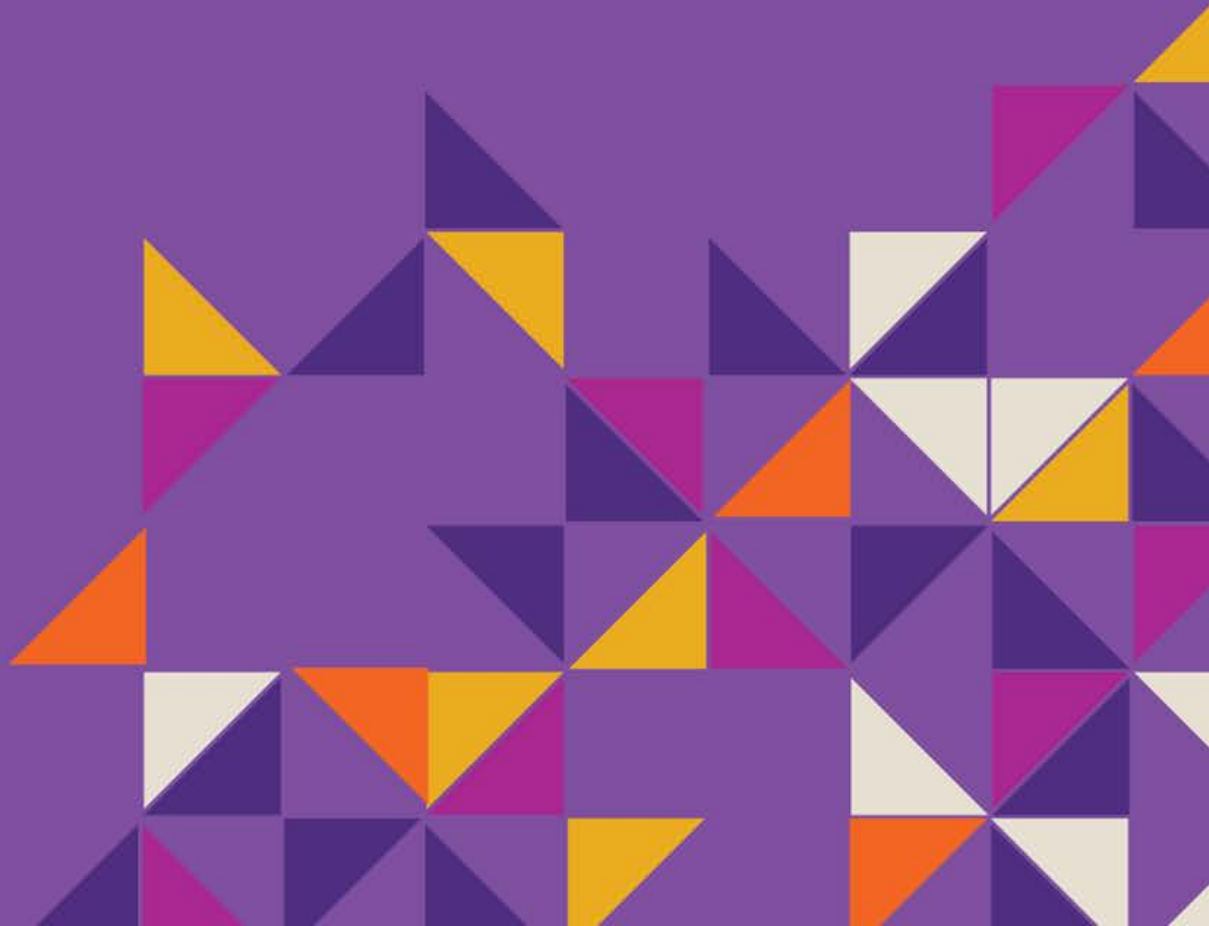
The current report on illicit trade in the retail sector has been broadened to include discussion, commentary and estimates in the alcohol, solid fuel and other sectors. The level of illicit activity which is under reported in these additional sectors is quite remarkable. Estimates for each sector have been revised and the estimates that we have provided show that illicit trade could be costing right holders as much as €1.56bn per annum and the Irish Exchequer circa €788m per annum.

We hope that this report will continue to inform and encourage active debate on the importance of tackling the scourge of illicit trade to the Irish economy. We will continue to engage with policy makers charged with practical and legislative changes which can bring about a substantial reduction in illicit activity.



Brendan Foster
Partner
Head of Consulting and Advisory

Executive summary



Executive summary

Illicit trade is continuing to develop in Ireland and is becoming a real threat to the Irish economy. This is Grant Thornton's third report on illicit trade in Ireland and focuses on the growing threat of illicit trade in the areas of alcohol, fuel, tobacco, pharmaceuticals, digital piracy and other product counterfeiting.

Overview

Illicit trade is continuing to show no signs of abating.

In 2015, we estimate that illicit trade could be costing the Irish economy as much as €2.35bn, as highlighted in Table 1 below.

The estimates that we have provided for the sectors covered in this report show that illicit trade could be costing right holders as much as €1.56bn per annum and the Irish Exchequer circa €788m per annum.

The non-financial impacts are as important as the financial impacts and must be considered also.

Non-financial impacts include health and safety concerns, undermining the legal and regulatory system, growth in organised crime, and reputational damage to brands.

In terms of the incentive for the supply and demand of illicit products, price remains the main driver of illicit trade.

Whilst there have been some efforts to improve legislation and enforcement across the sectors reviewed, the fundamental problem of unaligned, unbalanced and sector specific strategies continues to exist.

Alcohol

Illicit trade in alcohol involves the smuggling of alcohol products from countries with lower alcohol tax rates, excise duty fraud and the production/distribution of counterfeit spirits. The key driver for the illicit trade in alcohol products is the level of excise duty.

Increases in excise duties drive up the final price of local and imported alcoholic beverages which increases demand for cheaper products supplied by the illicit market.

Increased prices, as a result of increased excise, reduce the amount of registered alcohol consumption as consumers move towards cheaper products supplied by the illicit market.

The introduction of Minimum Unit Pricing (MUP) is currently being considered to eliminate cheap alcohol from supermarkets. The intention of MUP is to decrease the amount of alcohol consumed and decrease the harm caused by drinking alcohol. However, there are concerns from the industry that MUP will drive illicit trade activity as consumers will seek cheaper alternatives.

Seizures of alcohol continue to rise. Total seizure in Ireland has increased by 100% over the period 2010 to 2014. 550 seizures were reported in 2014, up from the 275 seizures in 2010.

Table 1: Cost to the economy

	Right holders/retailers lost revenues, €m	Government loss to Exchequer, €m	Total loss to the economy, €m
	Estimate	Estimate	Estimate
Fuel laundering	€196	€239	€435
Tobacco	€253	€197	€450
Pharmaceuticals	—*	€45	€45
Digital piracy	€320	€70	€390
Alcohol	€491	€165	€655
Other products	€300	€70	€370
	€1,560	€788	€2,345

*Figure difficult to estimate but industry sources suggest it could be in the region of €3bn.

Fuel

The introduction of the carbon tax in the Finance Act 2010 has had the direct effect of increasing prices for fuel products throughout Ireland. A noticeable fall out of these increases is the growth of illicit trade in solid fuel products such as coal, peat briquettes and sod peat. Perceived to be a victimless crime, this predominantly takes the form of cross-border fuel smuggling involving the illegal importing of solid fuel from Northern Ireland into Ireland.

In Ireland, the illicit trade in petroleum is principally in the diesel sector, as this offers the greatest potential for profit. Although fuel prices have been falling, changes in exchange rates and duties have resulted in increases in other illicit trade activities in this area, for example, petrol stretching and mixing.

Although it is difficult to reliably estimate the extent of losses incurred as a result of illicit trade in fuel, Revenue recognise that fuel fraud, including the laundering of markers from rebated fuel, is a significant threat to Exchequer revenue.

HM Revenue and Customs (HMRC) estimate that illegal diesel costs £80m in lost taxes and makes up 13% of the market share of diesel in Northern Ireland.

Recent estimates show a reduction in costs to the Irish economy from fuel laundering with losses to the Exchequer of €239m (2013: €261m) and losses to the industry of €196m (2013: €205m). These estimates do not take into account losses from other illicit trade in fuel activities or other financial and non-financial costs. As a result the costs to the economy and society are significantly greater than those highlighted in this report.

Tobacco

A key driver for the illicit trade in tobacco products is the level of excise duty. Criminals are attracted to the high profitability of this market as taxation policies across different jurisdictions give rise to opportunities for illegal traders to make profits by not paying domestic rates of duty.

From a demand perspective, increases in excise duties drive up the final price of cigarette products which increase demand for cheaper products supplied by the illicit market.

In Budget 2016, the excise duty on a packet of 20 cigarettes was increased by 50 cent (including VAT) resulting in each 20 pack now costing €10.50 compared to a cost of €8.55 in 2010.

On 10 March 2015, Ireland introduced The Public Health (Standardised Packaging of Tobacco) Act 2015. The aim of the legislation is to remove the marketing 'fashion element' from smoking to discourage children and young people taking up smoking. The new legislation bans all forms of branding such as trademarks and logos on packs of cigarettes, tobacco and cigars and introduces 65% health warnings on the packs. It is intended that these changes will begin to take effect from May 2016 and be fully in place by May 2017.

Concerns have been expressed by the tobacco industry and the international business community that the introduction of the plain packaging will have the effect of removing the protection of their brand and IP making products easier to counterfeit.

Revenue report that 11% of the cigarette market is from illicit trade a reduction from 16% recorded in 2009.

The tobacco industry considers these estimates to be significantly lower than the actual amount.

Excise receipts from tobacco have declined year-on-year between 2011 and 2014. In conjunction with this decrease was the year on year rise in the price of tobacco per 20 pack and a decrease in total sales by 13.8% during this period. In 2014 the percentage of non Irish duty paid cigarettes resulted in estimated losses of €253m to the industry and €197m to the Exchequer.

Pharmaceuticals counterfeiting

Price remains a key driver for the illicit trade in pharmaceutical products. Even with the price reductions in recent years, brought about by the introduction of generic medicines, representatives from users of medicines maintain that the price of medicines remains higher in Ireland than other European countries.

The spread of e-commerce has facilitated the purchase of illicit medicines in the market. Social media has also assisted in facilitating the purchase of falsified medicines in the market as sellers turn to these websites to advertise their products.

Cross-border travel is incentivised by lower priced medicines and the avoidance of the General Practitioners (GP) fee. There also remains a market for prescription medicines in Ireland that can be purchased without prescription in Northern Ireland.

Northern Ireland is also used as a convenient address to bypass regulatory controls in Ireland for the purposes of transiting abortifacients. Furthermore, it is reported that the postal system in the UK is increasingly being used by illegal traders to disguise the source of pharmaceuticals. Items coming from China, India etc. use the UK as a convenient postal address as it draws less attention to the illicit items than if their true source was stated.

Illicit trade in medicines in Ireland is different from some of the other areas discussed in this report. For the most part the illicit trade in medicines does not displace legitimate trade. This is because most of the illicit market which we see in Ireland does not qualify for prescription medicine supply and would not be available for purchase.

When we apply reported losses to the global pharmaceutical industry to the Irish market the loss suffered by the Exchequer and the industry is significant. Recent estimates indicate that Irish exporters have potentially suffered losses in the region of €3bn in 2014 and that losses to the Exchequer by way of corporation tax receipts are in the region of €45m. As with other estimates, the information available is limited and in reality the losses are likely to be higher.

Digital piracy

Digital piracy is a term used to describe illicit activities linked to a range of infringements on Intellectual Property Rights (IPR). It includes audio-visual piracy, software piracy and the theft of other electronically transmittable IP.

Digital piracy is perceived to be a victimless crime as little to no financial gain arises from the distribution of digitally pirated products online.

Due to the high numbers engaging in illegal downloading it is very difficult and uneconomical to pursue individual offenders.

Ireland's main copyright legislation is the Copyright and Related Rights Act 2000. This legislation is over 15 years old and is outdated considering the technological developments and changes in the online environment which have arisen since then.

Litigation is the vehicle typically used to curb illegal downloading but its success to date has been limited. As already mentioned, the legislation is dated and due to the high numbers engaging in illegal downloading it is very difficult and uneconomical to pursue offenders. In response, the affected industries have attempted to curb the supply by pursuing websites that facilitate the downloading of illegal content and forcing them to shut down, or restricting access to them through site blocking.

In terms of digital costs to the Irish economy, we estimate that in total:

- over 500 jobs were lost by 2015;
- retailers suffered losses of circa €320m in revenues; and
- the loss to the Exchequer in VAT receipts could be as much as €71m as a result of digital piracy.

Other product counterfeiting

Counterfeiting is the practice of manufacturing, importing and exporting, distributing, selling or otherwise dealing in goods, often of inferior quality, under a trademark that is identical to or substantially indistinguishable from a registered trademark, without the approval or oversight of the registered trademark owner.

The top categories of goods most commonly detained at EU external borders are sports shoes, clothing and bags, wallets and purses.

There is an increasing range of every day goods being counterfeited today.

Key drivers for the counterfeit market include:

- high profit margins:
 - profits made are based on brand value: high-brand products generate more lucrative returns so items in markets with high demand are normally chosen to counterfeit; and
 - lower production costs: there is no quality assurance or health and safety standards in the production of counterfeit products, resulting in lower production costs.
- consumers are easy to deceive: the products and packaging are of such a high quality that consumers may think the product is legitimate; and
- consumer demand for cheaper priced products.

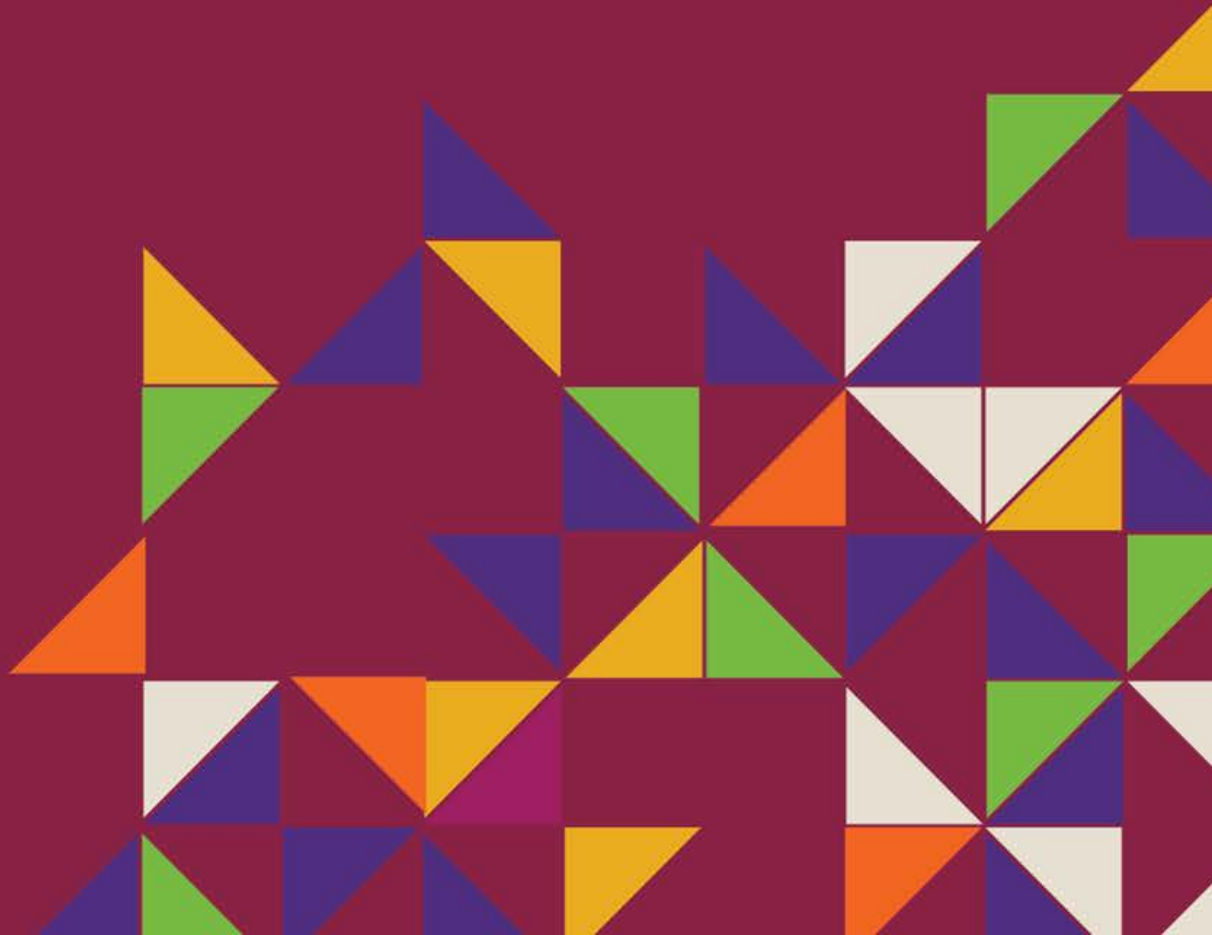
In 2008, the OECD estimated the total size of counterfeiting and piracy worldwide to be approximately US\$650bn. The Business Action to Stop Counterfeiting and Piracy (BASCAP) has updated this estimate for 2015 to a value of US\$1.7tr. This illustrates the alarming increase in this activity over a seven year period.

It is difficult to determine the costs of illicit trade on industry and on the Exchequer, especially given the market as it is largely unrecorded.

When we review counterfeit activities in isolation, the statistics would indicate an estimated loss in the order of €300m to industry and €70m in VAT receipts to the Exchequer.



Alcohol



Alcohol

Alcohol prices in Ireland are high as a consequence of high levels of excise tax duty. A stated objective of sustaining a high level of taxation is to reduce per capita consumption and the harms associated with excessive drinking. However, evidence suggests that high prices are linked to increases in illicit trade in alcohol and active cross-border shopping as consumers are reactive to price differentials. Current legislative and enforcement systems in Ireland in the area of illicit trade in alcohol do not act as a strong enough deterrent. In many instances, the benefits of undertaking illicit activities are considerably higher than the penalties and risks of being prosecuted.

The levels of illicit trade in alcohol products are lower when compared to tobacco, as alcohol is relatively expensive to produce and illicit activities generate a lower return. However, rising duties in alcohol will bring about an inevitable fall in revenue as counterfeit suppliers satisfy consumer demand for cheaper products¹.

What is illicit trade in alcohol?

Illicit trade in alcohol involves the smuggling of alcohol products from countries with lower alcohol tax rates, excise duty fraud and the production/distribution of counterfeit spirits.

The illicit trade is conducted in various ways. These range from 'classic' methods such as false customs declarations and/or accompanying documents, concealments in vehicles and containers, and the misuse of excise suspension regimes in the single markets².

Contributing factors to the illicit trade in alcohol products:

- Excise duties
Increases in excise duties drive up the final price of local and imported alcoholic beverages.
- Lower price alternatives
Smuggled alcoholic products are generally sold at lower prices to undercut legitimate alternatives.
- Government regulations
Government regulations concerning legal alcohol sales and consumption create more opportunities for the illegal market.
- Weak law enforcement
Weak law enforcement enables illegal activities.
- Access and availability
Access to and the availability of cheaper products facilitates the movement of illicit alcohol.
- Consumer perception
There is a certain level of acceptance and perceived legitimacy of contraband alcohol products.
Consumers perceive cheaper alcohol to be a bargain rather than it being counterfeit.

Key driver - the level of alcohol excise in Ireland

A key driver for the illicit trade in alcohol products is the level of excise duty. Increases in excise duties drive up the final price of local and imported alcoholic beverages which in turn increases demand for cheaper products supplied by the illicit market.

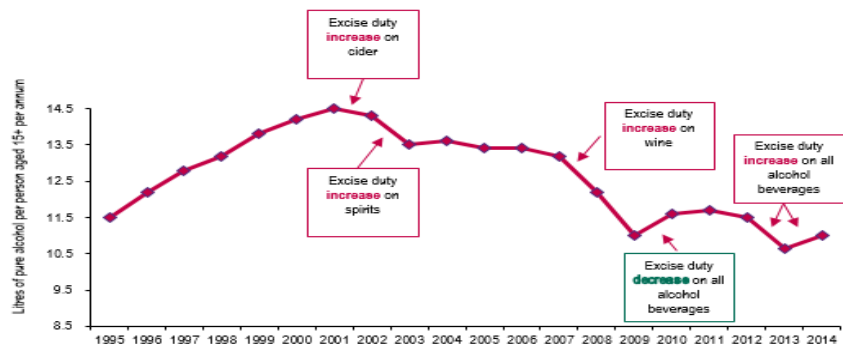
Ireland has higher levels of excise duty for all types of alcohol beverages when compared to other countries in Europe³. Apart from the UK, Sweden and Finland, most other countries have low alcohol excise.

In comparison Ireland has:

- the highest wine excise;
- the second highest cider excise;
- the third highest spirits excise (after Finland and Sweden); and
- the third highest beer excise (after Finland and the UK)⁴.

The impact that prices have had on smuggling and counterfeiting of alcohol is not unique to Ireland. Other countries with high excise levels have also been affected. For example, Sweden (high excise) has a problem of cheaper alcohol coming in from Denmark (low excise) who in turn has a problem with smuggled alcohol from Germany (lower excise)⁵.

Figure 1.1: Impact of excise duty changes on Ireland's alcohol consumption

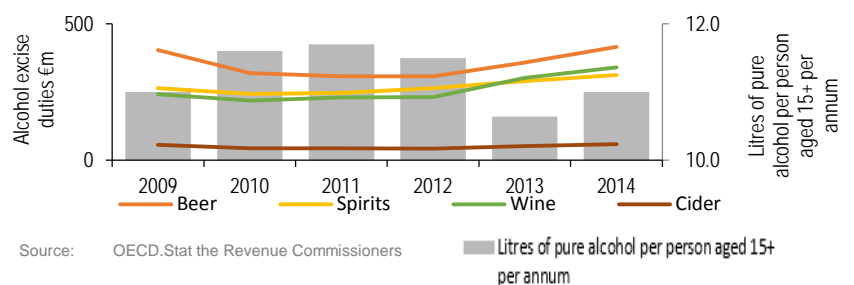


Source: OECD.Stat and the Minister for Health

Faced with an increase in prices, consumers respond by doing any of the following:

- drinking less;
- purchasing cheaper alcohol;
- switching from the on-trade to the off-trade;
- making savings elsewhere in the household budget;
- shopping abroad where the same alcohol can be purchased cheaper;
- brewing or distilling their own alcohol;
- buying counterfeit or smuggled alcohol products; and
- buying surrogate alcohol, for example, methanol.

Figure 1.2: Changes in alcohol product tax yield



Source: OECD.Stat the Revenue Commissioners

Increased prices, as a result of increased excise, reduce the amount of registered alcohol consumption as consumers move towards cheaper products supplied in the illicit market.

Receipts from alcohol excise in Ireland increased steadily from 2011 in response to the decrease in excise levels. This further strengthens the argument that excise increases result in lower priced illicit products being more attractive for the consumer, increasing illicit trade activities in this area.

Development – legislation

On 22 June 2015, the Irish Parliament (Oireachtas) Joint Committee on Health and Children published its report on the Pre-Legislative Scrutiny of the General Scheme of the Public Health (Alcohol) Bill 2015.

The legislation addresses ‘alcohol for the first time as a public health issue’⁶. The Bill includes provisions for the following:

- health labelling on alcohol products;
- MUP to eliminate cheap alcohol from supermarkets;
- advertising and marketing restrictions;
- regulation of sports sponsorship;
- structural separation in shops to reduce availability and visibility; and
- enforcement powers for environmental health officers.

In addition to health labelling the Committee recommends that the labelling should be standardised, taking into account best practice and guidelines.

Of the measures proposed there are concerns from the industry that MUP will increase the price of cheap alcohol and drive illicit trade.

Minimum Unit Pricing (MUP)

MUP works by setting a minimum price per gram of alcohol. The sale price of the alcohol product, in both the on- and off-trade sectors, cannot be below this minimum unit price.

The Government expects that the introduction of MUP, similar to increases in excise duty, will result in the amount of alcohol per capita decreasing and also a reduction in the harm caused by drinking alcohol.

However, according to key players in the alcohol industry there is a strong correlation between low affordability and higher rates of unrecorded alcohol consumption. Therefore, MUP is likely to have a greater impact on those with low affordability.

Although aimed at reducing consumption, dependent drinkers in this category are more likely to reduce spending and make savings elsewhere in the household budget so that they can maintain their alcohol consumption habits. The industry is concerned that MUP will drive illicit trade activity as people search for cheaper products.

Leo Varadkar
Former Minister for Health –
May 2015



“MUP is aimed at those who drink in a harmful and hazardous manner, and designed to prevent the sale of alcohol at very cheap prices.”

Christopher Snowden
Author of “Drinking in the
Shadow Economy”



“Minimum alcohol pricing might seem like a quick fix to tackle problem drinking, but it is likely to cause many more problems by pushing people towards the black market in alcohol.”

Counterfeit alcohol

Alcohol products are prime targets for counterfeiters due to their brand value and the high tax and excise component of the final price. These factors make them profitable products to counterfeit and sell on the illicit market.

Counterfeit components which go into making the products are items such as raw alcohol (methanol), a substitute for ethanol which is used in genuine alcohol products, and packaging i.e. bottles, bottle caps and labelling. According to Revenue this counterfeit alcohol is difficult to spot as genuine bottles are used, having been sourced from pubs and recycling centres⁷.

Spirits (vodka) are the most common category of alcohol to be counterfeited, having been bottled and packaged to resemble the genuine product. In addition, there are indications that counterfeit wine is also becoming increasingly available⁸.

In an effort to increase margins publicans may purchase counterfeit products at cheaper prices, not realising that they are not genuine. Unsuspecting consumers looking for a bargain may have trouble distinguishing a genuine product from one that is counterfeit and potentially harmful.

Counterfeit alcohol has been detected in bars and off licences in Ireland, often having been made locally at illegal bottling plants. A report carried out by the PSNI and An Garda Síochána supports this, commenting that “*cross border activities are clearly present with a particular concentration of illegal bottling plants/ distribution points identified in the border region*”⁹.

Aside from the losses suffered by manufacturers, retailers and the Exchequer, counterfeit alcohol also poses major health risks to consumers. There is no quality control as the products are not tested. In many cases the alcohol is sourced from the industrial alcohol sector and may contain high quantities of methanol rather than ethanol which is found in genuine alcohol products.

“We would reiterate that cheap alcohol from an irregular source is likely to be counterfeit and could potentially cause serious harm if consumed”

Source: Quote from the Revenue Commissioners to Drinks Industry Ireland



Cross-border issues with Northern Ireland

There are significant price differentials between alcohol prices in Ireland and Northern Ireland. Taxation policies are largely responsible for these differentials and provide incentives for illicit trade and cross-border shopping.

Price differentials

Driven by taxation policies the price differentials, particularly in relation to spirits and wines, are outlined in Table 1.1 below. This table illustrates how bulk buying by domestic consumers engaging in cross-border shopping can result in substantial consumer savings.

The greatest differences in price differentials are seen in particular with spirits (vodka and whiskey) and wine (chardonnay and sparkling) which are more expensive in Ireland.

Cross-border cooperation

The authorities in Ireland and Northern Ireland currently cooperate on a range of cross-border issues, including illicit trade in alcohol products. Their greatest law enforcement challenge is cross-border smuggling and illicit trade, with “*an all island approach required to adequately deal with illicit trade*”¹⁰.

There are concerns from the industry about the impact that MUP might have in terms of increasing cross-border illicit trade. In addition to legislation being introduced in Ireland, the Minister for Health in Northern Ireland has also announced plans to introduce MUP. Alignment of pricing between both jurisdictions however is difficult and may not work in practice as this would require:

- setting of prices to the same level. This would require Northern Ireland to significantly increase the price of some product lines which would not be welcomed by the public and therefore likely to be rejected; and
- constant adjustment to reflect any changes in the euro/sterling exchange rate.

These measures would reduce the instances of cross-border illicit trade. However, they could also result in consumers purchasing cheaper illicit and/or counterfeit alcohol from other markets to satisfy their demand.

Table 1.1: Alcohol price comparison between ROI and NI

Alcohols	Price ROI €	Price NI €	Price variance €	Total tax ROI €	Total tax NI €	Tax variance €	Total tax as a % of price ROI	Total tax as a % of price NI
Stout (500ml)	2.00	2.20	(0.20)	0.85	0.89	(0.04)	42.5%	40.5%
Lager (500ml)	1.95	1.95	-	0.85	0.92	(0.07)	43.6%	47.2%
Lager (330ml)	1.50	1.35	0.15	0.60	0.58	0.02	40.0%	43.0%
Vodka (bottle)	20.00	18.22	1.78	14.91	12.84	2.07	74.6%	70.5%
Whiskey (bottle)	27.34	26.26	1.08	17.03	14.84	2.19	62.3%	56.5%
Wine - Chardonnay	11.70	10.04	1.66	5.37	4.44	0.93	45.9%	44.2%
Wine - Sauv. Blanc	8.50	9.98	(1.48)	4.78	4.43	0.34	56.2%	44.4%
Sparkling Wine	18.07	14.29	3.78	9.75	5.93	3.82	54.0%	41.5%

Source: 1. Revenue Commissioners price comparison survey, 7 May 2015 [X]

Enforcement

Action by the authorities to combat the illegal trade of alcohol targets all stages of the supply chain. From an international perspective, Operation Opson IV, a Europol/Interpol international operation conducted during December 2014 and January 2015, resulted in nearly 275,000 litres of alcoholic produce being seized. Also seized were “more than 20,000 empty bottles ready for filling, hundreds of empty five-litre antifreeze containers which had been used to make the counterfeit alcohol, as well as a reverse osmosis unit used to remove the chemical’s colour and smell”¹¹.

In Ireland, the number of seizures of counterfeit and non-duty paid alcohol in Ireland is on the rise, having increased by 100% from 275 seizures in 2010 to over 550 seizures in 2014. However, there are growing reports of counterfeit spirits being sold by both licit and illicit retailers and, although detections have continued to increase, prosecutions have remained static over recent years.

Current legislative and enforcement systems in Ireland in the area of illicit trade do not act as strong enough disincentives. In many instances the benefits of undertaking illicit activities are considerably higher than the penalties and risks of being prosecuted. The strengthening of enforcement tools such as trademarks and greater penalties would create more effective and durable deterrents against counterfeiters.

Key facts and figures

-  Illicit alcohol seizures in Ireland have increased by 100% from 275 in 2010 to 550 in 2014.
-  Greater law enforcement is required to act as a deterrent.
-  Counterfeit alcohol was among the most seized product in Operation Opson IV (2015).
-  There are growing reports of counterfeit spirits being sold by both licit and illicit retailers.
-  Detections continue to increase, prosecutions remain static.

Table 1.2: Alcohol detections and seizures 2010 to 2014

	2010	2011	2012	2013	2014	Variance 2010 to 2014 %
Number of seizures	275	361	355	507	550	100.0%
Litres	43,498	32,196	32,834	55,755	40,237	(7.5)%
Value (€m)	0.60	0.50	0.70	1.5	0.6	0.0%

Source: Revenue Commissioners

Figure 1.3: Prosecutions for alcohol offences for sale or delivery of products on which no excise had been paid



Source: Revenue Commissioners

“Counterfeiters have little to fear from such anti-smuggling techniques and governments can do little about home distilling or the covert production of illicit alcohol”. National Audit Office (UK), 2012



Cost to the economy

The World Health Organisation (WHO) has estimated that around 30% of all alcohol consumed globally is illegally produced or ‘unrecorded’.

However, the consumption of unrecorded alcohol from the illicit trade market is by its nature difficult to measure. In Ireland it is likely that this percentage is much lower.

Illicit alcohol seized in 2014 was 40,237 litres. Assuming this comprises of spirits, an Alcohol by Volume (ABV) of 40% is applied to it.

When compared to the 39.53 million litres of pure alcohol consumed in Ireland in 2014, this amount represents just 0.04% of the alcohol consumed in Ireland last year¹².

Estimated losses to the Exchequer, range from €110m to €219m. Potential losses suffered by the industry by way of lost revenues range from €327m to €654m.

In the UK, the HMRC estimated in 2012/13 that the alcohol tax gap could be as much as £1.2bn per annum – 13% of a total annual tax revenue of over £9bn – including avoided excise duty and illicit alcohol.

Other costs to the economy

In 2014, the drinks industry contributed over €2,193m in VAT and excise to the Exchequer, not including other contributions from income tax, corporation tax and PRSI receipts.

It is reported that alcohol excise increases in recent years have cost the sector thousands of jobs, with over 1,000 pubs throughout Ireland having been forced to close since 2007¹³.

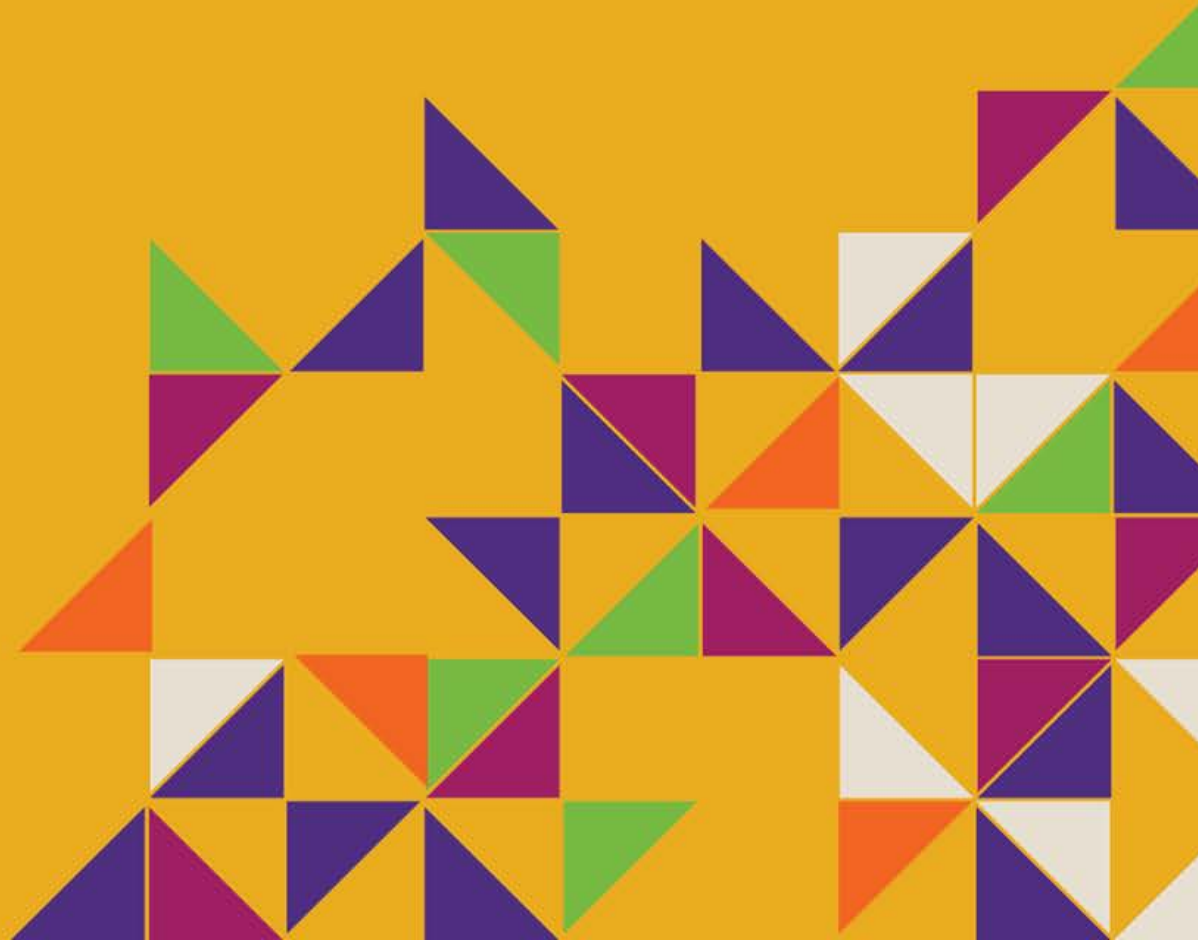
Counterfeit and smuggled alcohol activities also impact the public by way of health and public order. Counterfeit alcohol can contain potentially life threatening levels of dangerous ingredients, whilst alcohol smuggling is linked to other illegal activities such as money laundering and drug dealing.

Table 1.3: Estimate of the loss to the Exchequer and industry from the illicit trade in alcohol

	2014	
Millions of litres of pure alcohol consumption	39.53m	
Population aged 15 and over (millions)	3.59m	
Litres of pure alcohol per adult	11	
Market size - consumer spend on alcohol	€6,542m	
Total VAT and excise receipts	€2,193m	
Illicit trade %	Low - 5%	High -10%
Estimated loss to the Exchequer	€110m	€219m
Estimated loss to Industry	€327m	€654m

Sources: CSO; OECD.Stat, Minister for Health, Department of Finance, DIGI and Grant Thornton analysis

Solid fuel



Solid fuel

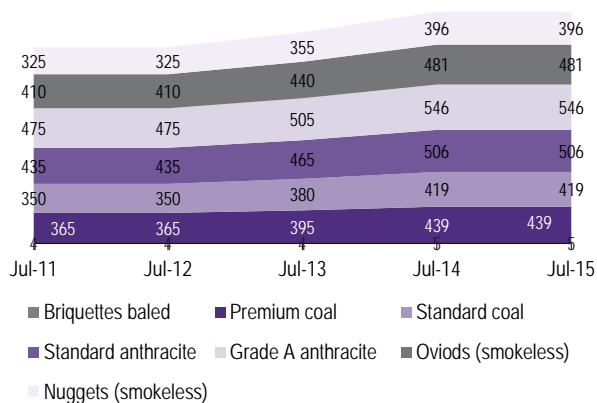
The introduction of the carbon tax in the Finance Act 2010 has had the direct effect of increasing prices for fuel products throughout Ireland. A noticeable fall out of these increases is the growth of illicit trade in solid fuel products such as coal, peat briquettes and sod peat. Perceived to be a victimless crime, this predominantly takes the form of cross-border fuel smuggling involving the illegal importing of solid fuel from Northern Ireland into Ireland.

Key driver: the price of solid fuel in Ireland

The Irish residential solid fuel sales market per annum is estimated to be 410,000 tonnes for coal products, 203,000 tonnes for peat briquettes and 700,000 tonnes for sod peat¹⁴.

Total demand for solid fuel is no longer on the rise. However, because of its impact on the atmosphere and Ireland's taxation policies, the price is rising. The increase in prices does not translate across into Northern Ireland where, with a lower VAT rate and no carbon tax, solid fuel is considerably cheaper, thus creating an incentive for cross-border fuel smuggling.

Figure 2.1: SEAI: Domestic fuel costs in Ireland (average price per unit (€))



Source: Energy in Ireland Key Statistics 2014*, SEAI

Carbon tax and solid fuel

In the Finance Act 2010, carbon tax was introduced “to support emission reduction, reduce demand for high carbon fuels and encourage substitution to low-carbon alternatives”.

The introduction the carbon tax was deferred until 2013 when a more ‘robust mechanism’ would be in place to protect against illegal imports. It was fully implemented in Ireland in a two phase application approach:

- phase one: 1 May 2013 at €10 per tonne of CO² emitted; and
- phase two: 1 May 2014 at €20 per tonne of CO² emitted.

Although the carbon tax has been implemented in full, there is no evidence that the promised ‘robust mechanism’ to protect against illegal imports is yet in place¹⁵.

However, what is certain, is that the introduction of the carbon tax has directly increased prices. This is illustrated in Table 2.1 which outlines the rates of tax applied.

Table 2.1: Carbon tax rates on solid fuel

Solid fuel type	Rate of tax at 1 May 2013 Carbon tax per tonne €	Rate of tax at 1 May 2014 Carbon tax per tonne €
Coal	€26.33	€52.67
Peat briquettes	€18.33	€36.67
Other peat	€13.62	€27.25

Source: Revenue Commissioners

Cross-border fuel smuggling

The residential solid fuel market is predominantly a cash business with few barriers to entry¹⁶. Products are easily transported and stored. They require no specialised storage and handling and are generally packed in small size packaging. For example, coal is typically packaged in bags of 40kg and peat briquettes in packs of 12.5kg. These characteristics, coupled with the open border between Northern Ireland and Ireland and the wide availability of solid fuel, make it easy to exploit price differences for profit.

As illustrated in Table 2.2, a comparison of the tax regimes in Northern Ireland and Ireland and the resulting impact on prices of solid fuel demonstrates that there are incentives for illicit trade activities in this area. Northern Ireland, with no carbon tax and a lower VAT rate of 5%, has significantly lower prices than Ireland. To illustrate, a truck carrying 26 tonnes of coal is €2,217 more expensive in Ireland (see Table 2.3). The potential savings from purchasing solid fuel in Northern Ireland is therefore a powerful incentive for illicit activity.

Table 2.2: Comparison of tax regimes in the ROI and NI on prices of solid fuel

	ROI	NI
VAT rate	13.5%	5.0%
Carbon tax charged?	YES	NO
Carbon tax per 40kg bag of coal	adds €2.11 to the price (€2.40 incl. VAT)	adds £0
Carbon tax per bale of briquettes	adds €0.46 to the price (€0.52 incl. VAT)	adds £0
Carbon tax per tonne of sod peat	adds €27.25 to the price (€30.93 incl. VAT)	adds £0

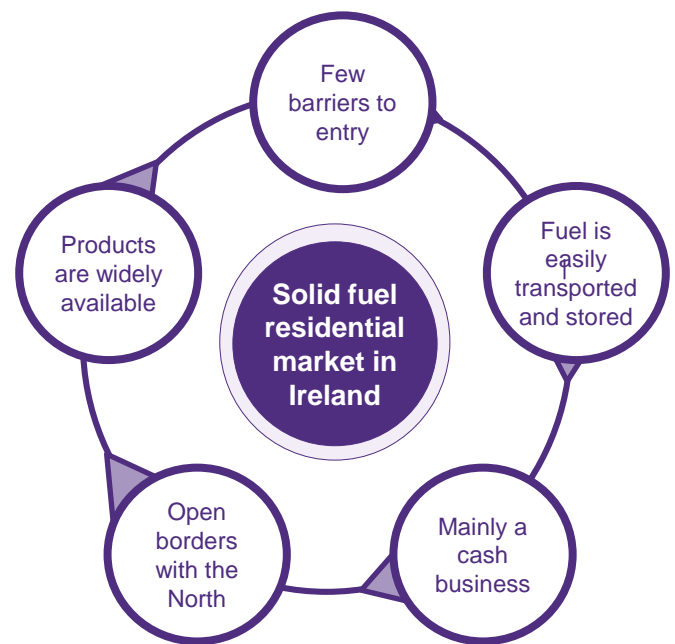
Source: Revenue Commissioners

Table 2.3: Worked example: Truck carrying 26 tonnes of coal price comparison NI versus ROI

	ROI	NI	Difference
Cost*	€7,800	€7,800	-
Carbon tax	€1,369	n/a	
Subtotal	€9,169	€7,800	€1,369
VAT %	13.5%	5.0%	
VAT €	€1,238	€390	€848
Total cost	€10,407	€8,190	€2,217

Note: *As coal is internationally traded, the cost is the same for both ROI and N.Irl.
Source: Revenue Commissioners and Grant Thornton analysis

Figure 2.2: Characteristics of the solid fuel market in Ireland which contribute to the illicit market.



Impact on the economy

Similar to illicit trade activities carried out in other sectors, it is difficult to estimate the size of the market in solid fuel smuggling. Revenue, who are responsible for the collection of the solid fuel carbon tax, are aware that illicit trade activities with regards to solid fuel exists. They too have no reliable way to estimate the size of this shadow economy.

Some trade sources have estimated that the combined VAT and carbon tax could drive coal imports to 30% of the total coal market (c100 kilotonne of oil equivalent per annum)¹⁷.

If we apply this percentage across the residential solid fuel market this would equate to a loss in carbon tax revenues to the Exchequer of over €9.5m (excluding VAT receipts).

Table 2.4: Residential fuel market carbon tax estimate - coal and peat products

Year: 2013	Ktoe	Conversion factor*	Tonne (000's)	Carbon tax rate/tonne €	Carbon tax €000's
Coal products					
Coal	173	0.665	260	52.67	13,702
Antracite and ovoids	83	0.665	124	52.67	6,573
Lignite	17	0.665	25	52.67	1,346
Total residential coal products	273				21,622
Peat products					
Peat briquettes	90	0.443	203	36.67	7,449
Sod peat**	128	0.313	408		
Sod peat traded est.			100	27.25	2,725
Total residential peat products	218				10,174
Total carbon tax (assuming no tax liability on 308,946t of Sod peat - untraded)					31,797
Illicit trade estimate: 30% of the market illicit					
Loss to the Exchequer					9,539
Loss to the industry					88,757

Source: SEAI, Revenue Commissioners and Grant Thornton analysis

In addition to loss of revenues to the Exchequer and to the industry, the economy is likely to be impacted by potential job losses from the introduction of carbon taxes and the resulting incentivised illicit activities.

- the Solid Fuel Trade Group (SFTG), a representative body of the industry, have expressed concerns that the absence of a robust method to stop untaxed products coming into the marketplace could result in an estimated loss of 320 jobs to the industry; and
- the Irish Hardware and Builders Merchants Association further estimate that 5% of jobs in that sector could also be lost, the equivalent of 1,200 jobs.

Enforcement

Seizures and detections

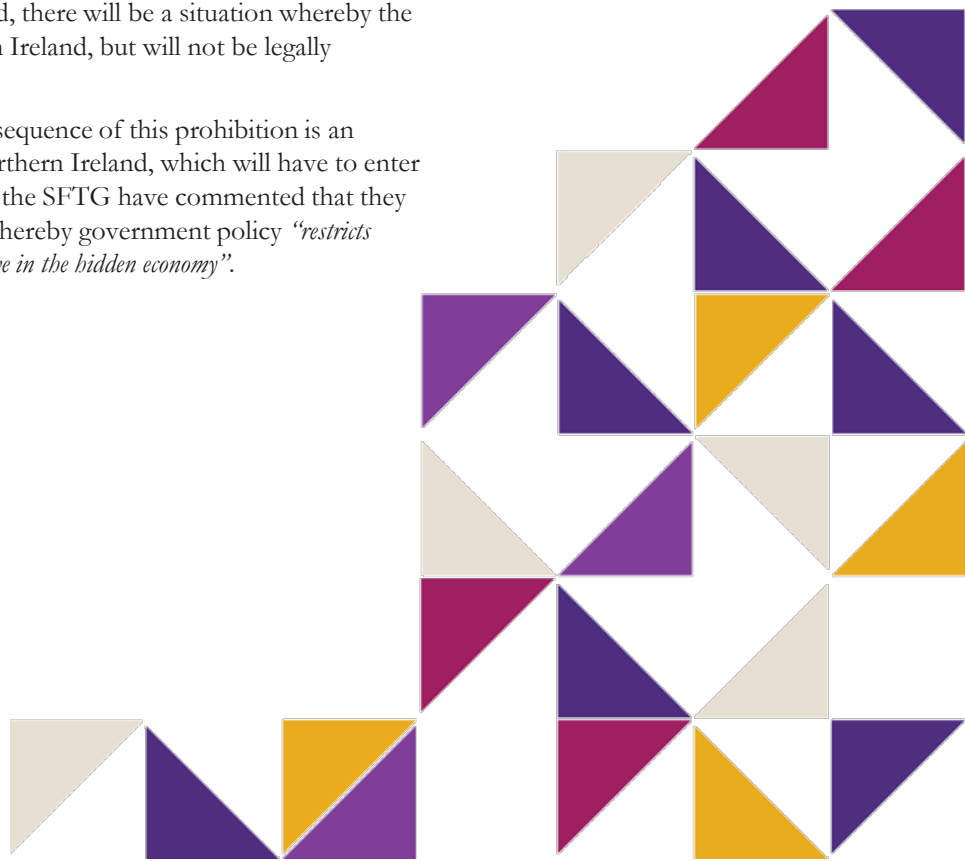
Seizures are uncommon as it is very difficult to prove the source of solid fuel or to prove intent to distribute it. Due to recent growth in the area of illicit trade in solid fuel, recommendations have been put forward by the industry with regards to carbon taxes and cross-border solid fuel smuggling. These recommendations include:

- auditing of fuel suppliers by Revenue. This will create an environment of greater compliance;
- obtaining of records from fuel suppliers based in Northern Ireland by Revenue and HMRC, identifying who has been supplied within Ireland. Every end user and fuel supplier who bought products in Northern Ireland needs to receive a communication from Revenue requesting evidence of carbon tax compliance;
- a coordinated multi-disciplinary approach comprising Revenue, HMRC, An Garda Síochána, PSNI and the enforcement teams from the respective Departments of Environments in Northern Ireland and Ireland;
- registration of all solid fuel traders, with associated obligations to submit bi-monthly carbon tax returns. The Return of Oil Movements (ROM) system introduced for petroleum oil suppliers should be used in the solid fuel market;
- clarification regarding personal imports. It is not clear to end users that they cannot import solid fuel without paying carbon tax if they do not personally accompany the fuel across the border for their own domestic use. Revenue needs to have a public awareness campaign; and
- spot checking of fuel transporters on the roads for compliance with carbon tax and VAT legislation.

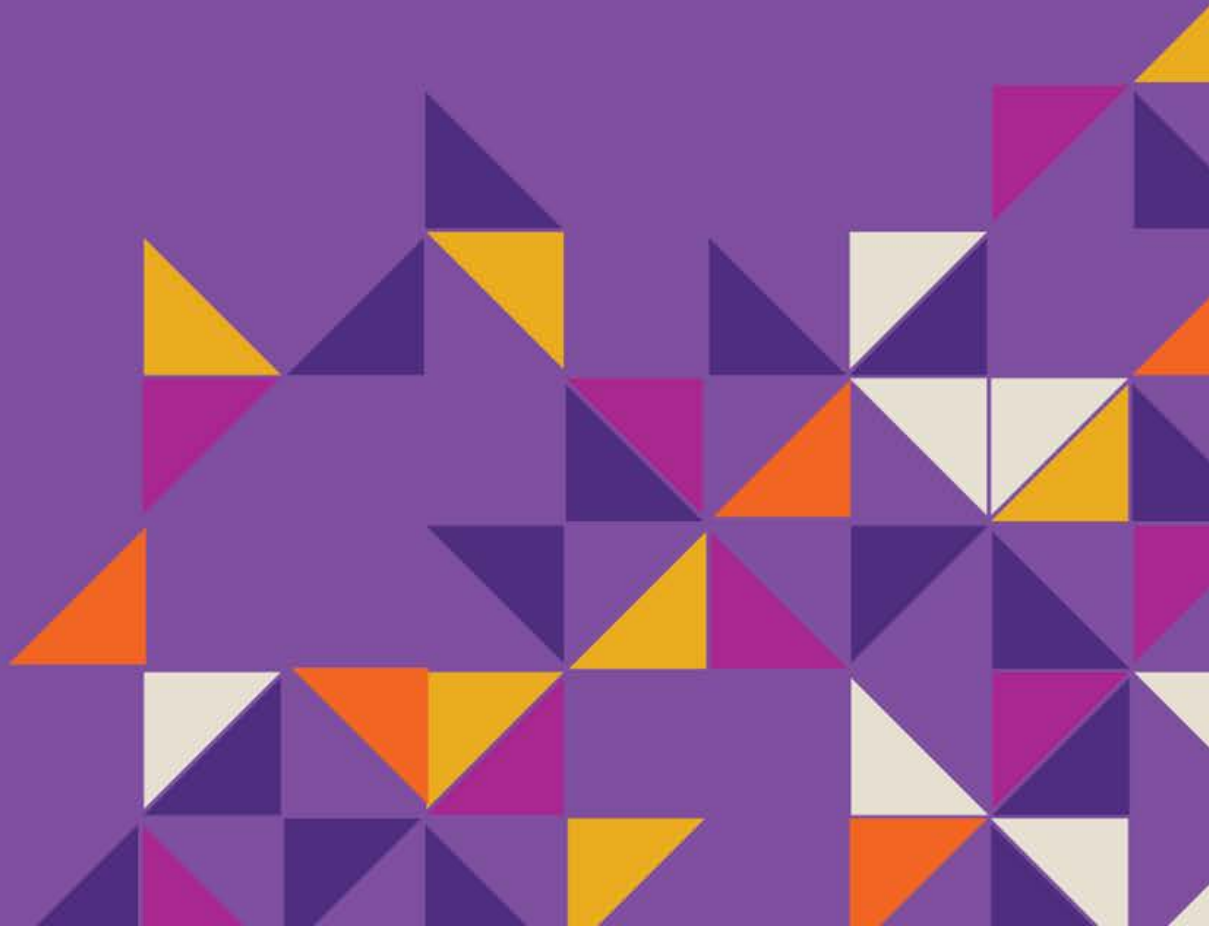
Developments - legislation

On 29 September 2015, the Minister for Environment, Alan Kelly TD, announced that by 2018, the bituminous coal ban currently enforced throughout major towns in Ireland is to be extended nationwide. If this is to proceed, there will be a situation whereby the product will continue to be available in Northern Ireland, but will not be legally available in Ireland.

The industry is concerned that an inevitable consequence of this prohibition is an increase in demand of bituminous coal from Northern Ireland, which will have to enter the market unofficially. Industry representatives, the SFTG have commented that they are of the opinion that this is another example whereby government policy *“restricts legitimate business, whilst simultaneously creating incentive in the hidden economy”*.



Petroleum




Petroleum

There are four main types of illegal fuel related activities: smuggling, mixing, stretching and fuel laundering. Most of these involve the passing off of illegal fuel as legitimate product for sale at discounted rates to unsuspecting fuel retailers and/or motorists.


The activity which traditionally provides the greatest threat to the economy both north and south of the border and is the focus of this report is that of diesel fuel laundering. This is because fuel laundering continues to offer the greatest financial incentive to criminals in Ireland.

In Ireland, illicit trade in petroleum is principally in the diesel sector, as this offers the greatest potential for profit. The diesel market is in a state of transition, having experienced both reductions in demand from the freight sector and increases in demand from a significant shift from petrol to diesel in the car market. Although fuel prices have been falling, changes in exchange rates and duties have resulted in increases in other illicit trade activities in this area, for example petrol stretching and mixing.


Types of illegal fuel related activities


Fuel laundering  Fuel laundering is the illegal process which removes the marker dye (red in the UK and green in the ROI) contained in agri-diesel. It is then sold/ passed off as regular diesel and a higher margin achieved.

Red (UK) and green (ROI) diesel is cheaper than regular diesel and is intended for off-road agricultural use.

Petrol stretching  Petrol stretching, or adulterated petrol, involves adding up to 10% of a product which would attract less duty to it before selling on to the service station and then on to the motorist.

Kerosene (which is used for domestic heating purposes) has been reported to be the most common product used for this purpose.

Smuggling  The border between Ireland and Northern Ireland provides opportunities for criminals to benefit from cross border sales, profiting from the differences in duties and exchange rates that exist at that time.

Mixing  Mixing involves combining duty rebated fuel with non-duty rebated fuel.

Key driver – price

The price of diesel in Ireland continues to be a key driver for illicit trade. The price differential between auto-diesel and agri-diesel at €0.55 per litre remains a strong incentive for laundering diesel. This gap is driven by different excise levels and VAT rates charged.

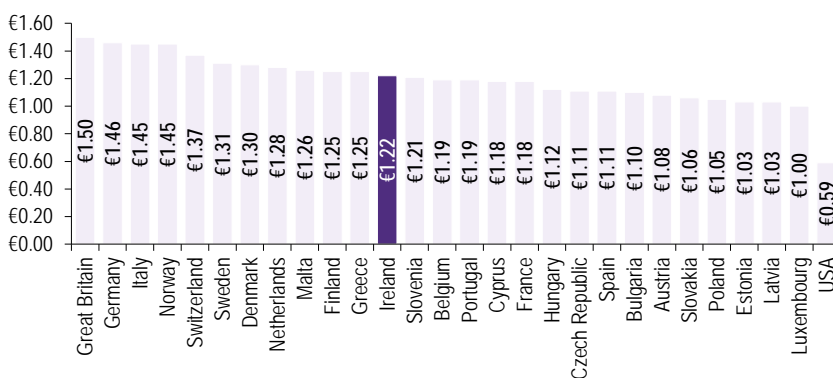
Table 3.1: Price comparison per litre: auto-diesel versus agri-diesel

	Auto diesel	Agri-diesel	Difference
Pump price	€ 1.29	€ 0.75	€ 0.55
	Auto diesel	Agri-diesel	Difference
Pre-tax price	€ 0.55	€ 0.53	€ 0.02
Excise duty (incl. carbon)	€ 0.48	€ 0.10	€ 0.38
Nora	€ 0.02	€ 0.02	-
VAT (23%/13.5%)	€ 0.24	€ 0.09	€ 0.15
Total taxes	€ 0.74	€ 0.21	
Tax as %	57%	28%	
Price	€ 1.29	€ 0.75	€ 0.55

Source: AA Ireland, IFA's quarterly fuel price survey June 2015 and Grant Thornton analysis

In September 2015, Ireland had the twelfth highest price in the EU at the pump for diesel at €1.22. This is an improvement on figures reported in January 2014 in which Ireland had the sixth highest price at €1.48. Although prices have reduced over the period, agri-diesel still remains significantly less at €0.75 per litre.

Figure 3.1: Diesel pump prices across the EU



Source: AA Ireland (September 2015)

The financial incentive for illegal traders

The Irish Petroleum Industry Association (IPIA) estimate the following gains can be made by illegal traders with respect to fuel laundering and petrol stretching:

- fuel laundering: the benefit to the illegal trader is that just one 38,000 litre load of washed off-road diesel could generate €20,000 to the criminal; and
- petrol stretching: it is estimated that the trader can make up to €700 extra for every 10,000 litres of petrol they sell.

Development - legislation

Recent legislative developments in the Finance Acts have seen the strengthening of Revenue powers and also increased emphasis on supplier responsibility when it comes to the area of illicit trade in fuel:

- Finance Act 2014 saw the strengthening of Revenue's powers to revoke a petroleum trader's license where the trader does not comply with excise law; and
- Finance Act 2013 included a provision which makes the supplier of marked fuel which is the subject of fraud liable to the fuel duty.

Developments - fuel laundering

Introduction of the colourless diesel marker

A colourless diesel marker was introduced in April 2015 throughout the island of Ireland. The marker is in addition to existing markers added to the fuel and is a joint project with Revenue and HRMC who will share information to help identify those dealing in illicit fuel.

It was introduced into supplies in April 2015. It is hoped that the new marker will make marked diesel uneconomic to launder¹⁸.

In addition, a full programme of fuel testing using new fuel analysers has also been rolled out. The new roadside fuel testing equipment permits officers to test vehicles at the roadside for the presence of the new fuel marker.

Traceability scheme - the monthly return of oil movements

From January 2013, people involved in the trade must submit a monthly ROM.

This traceability scheme provides the opportunity for Revenue to have full visibility of fuel purchases and sales in the country. In addition, analysis carried out on the returns assists Revenue in the identification of any loop-holes and scams. *"If you buy 36,000 litres of green diesel you have to account for it"*¹⁹.

It is reported that already this legislation has had a positive affect and has started to put illegal operators out of business.

"I am delighted to see first-hand the new roadside testing equipment in action. Together with the new marker it will play an important part in the fight against fuel fraud."

Exchequer Secretary to the HM Treasury, Damian Hinds



Cross-border issues with Northern Ireland

Price differentials as a result of duty and movements in exchange rates make smuggling fuel from one side of the border to the other attractive at various times.

The open border between the Northern Ireland and Ireland provides opportunities for criminal gangs on both sides of the border to benefit from cross-border sales. In addition, the criminals in this area “have a history, they know the border area well and they know how to make their money”²⁰.

Fuel laundering plants

According to Revenue and Customs there are circa ten or twelve main gangs that continue to launder fuel both north and south of the border. In Northern Ireland, laundering plants continue to be found in significant numbers. In 2013, HMRC detected and dismantled 38 illegal laundering plants in Northern Ireland and seized a total of 574,238 litres of fuel. Between January and August 2014, an additional 16 were discovered²¹.

Petrol stretching

Incidences of petrol stretching are reported to be on the rise. Revenue received a total of 138 complaints for the period from July 2014 to April 2015, the majority of which originated in Revenue's Border Midland West (BMW) region.

Managing the border area

Managing the border area is very difficult. Many of these criminals have been working in organised gangs for many years and know the system well. *“If we take down a laundry up here they will just move it somewhere else, normally north of the border. If they are caught up in the north they'll move down here. It's a difficult area to police”*. (Sean Kelleher, Manager, Revenue Customs).

Although this activity is mainly concentrated along the border, there has been a movement away from this area in both Northern Ireland and Ireland. Over the past year, laundering operations were found in Dublin, Waterford, Coalisland, Co. Tyrone and Banbridge, Co. Down²².

Table 3.2: Price differentials between the Northern Ireland and Ireland

Petroleum products	Price in Ireland€	Price in NI €	Price Difference €	Total Tax/Duty in Ireland€	Total Tax/duty NI€	Difference Total Tax/duty €	Total tax as a % of price in Ireland	Total tax as a % of price in NI
Unleaded petrol (one litre)	1.46	1.69	(0.23)	0.86	1.10	(0.24)	58.9%	65.1%
Auto diesel (one litre)	1.31	1.68	(0.37)	0.72	1.10	(0.38)	55.0%	65.5%
Kerosene (one litre)	0.64	0.50	0.14	0.13	0.02	0.10	19.9%	4.8%
Agri diesel (one litre)	0.70	0.70	0.00	0.19	0.19	(0.01)	26.5%	27.3%
Difference: auto 'v' agri diesel	0.61	0.98						

Source: Revenue Commissioners price comparison survey, 23 July 2015

Enforcement

Detections and seizures

Excisable products seized in recent years have decreased from 718K litres seized in 2011 to 151K litres in 2014 according to data from Revenue.

This indicates a much-reduced incidence of laundered fuel on the market as commercial seizures have decreased from 88 to 32 during the same period.

Road diesel consumption and tax revenues have risen significantly compared with a couple of years ago. Revenue figures demonstrate that diesel clearances rose 5% in 2013 and 6.3% in 2014 which indicates that, aside from what would be expected from the change in market demand, Revenue initiatives have impacted consumption and boosted the amount of legitimate sales²³.

While other economic factors have contributed to this growth in tax revenues, reduced fraud is also an important factor.

It is not clear however the impact of laundered diesel in the overall market.

Cross-border cooperation

The authorities in Ireland and Northern Ireland continue to work together to find ways to combat fuel laundering.

The Cross-Border Fuel Fraud Enforcement Group, a multi-agency special cross-border force, was set up with the primary focus of tackling this problem.

The BIPA assembly report, discussed earlier in this report, welcomed the development of this task force.

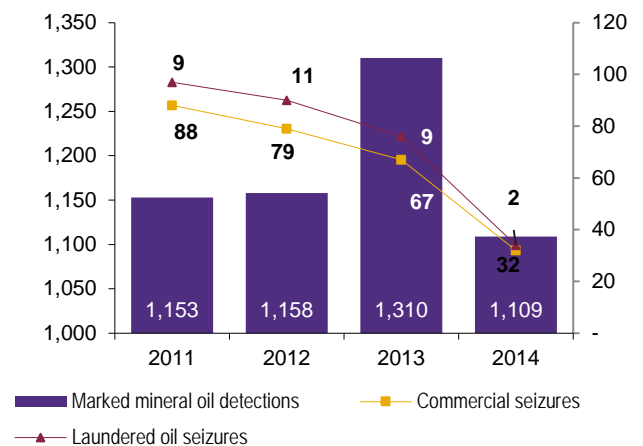
Resources remain limited however. One of the key recommendations made was that the Cross-Border Enforcement Groups “establish a permanent, full time task force dedicated to eliminate activities of organised crime gangs involved with cross-border illicit trade”.

Table 3.3: Detections, seizures and convictions: 2011 to 2014

	2011	2012	2013	2014
Marked mineral oil				
Detections (number)	1,153	1,158	1,310	1,109
Commercial seizures (number)	88	79	67	32
Commercial seizures (volume-litres)	718,181	876,887	771,232	150,800
Convictions (number)	218	207	228	283
Laundered oil				
Seizures (number)	9	11	9	2
Volume (litres)	326,649	199,055	103,650	50,340
Convictions	2	2	*n/a	4
Vehicle seizures				
	162	114	174	154

Source: Revenue

Figure 3.2: Detections and seizures: 2011 to 2014



Cost to the economy

Although it is difficult to reliably estimate the extent of losses incurred as a result of illicit trade in fuel, Revenue recognises that fuel fraud, including the laundering of markers from rebated fuel, is a significant threat to Exchequer revenue.

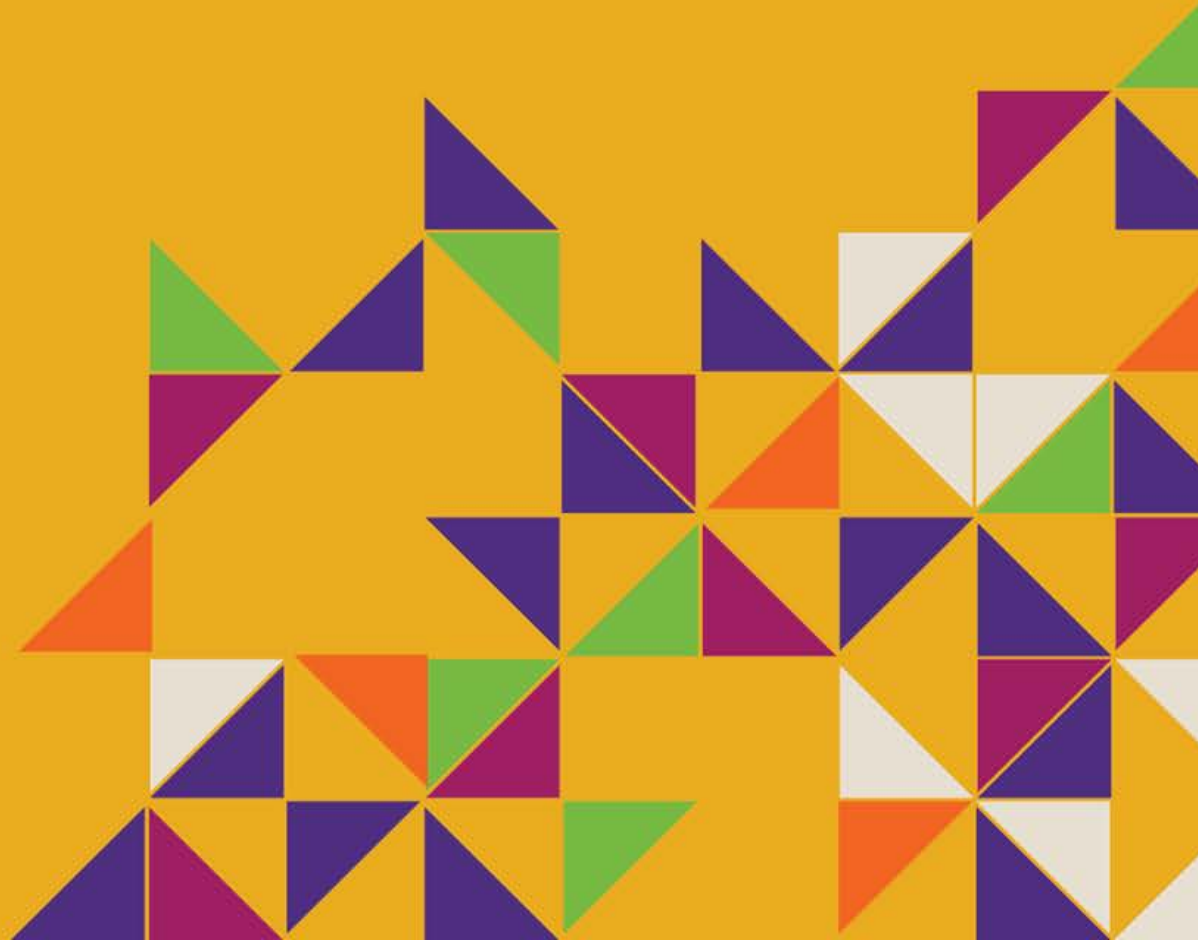
The sale of laundered diesel continues to cause losses to the Exchequer directly in excise duty, VAT and carbon charges. Losses to the Exchequer are not only the financial cost of illicit trade in fuel. Other costs such as the clean-up of toxic waste generated from fuel laundering activities, enforcement, and the costs to retailers are all significant and need to be considered when assessing illicit trade in fuel.

The HM Revenue and Customs estimate that illegal diesel costs £80m in lost taxes and makes up 13% of the market share of diesel in Northern Ireland.

Updated estimates show a reduction in costs to the Irish economy from fuel laundering with losses to the Exchequer of €239m (2013: €261m) and to the industry of €196m (2013: €205m). These estimates do not take into account losses from other illicit trade in fuel activities or other financial and non-financial costs. As a result the costs to the economy and society are significantly greater than are highlighted in this report.



Tobacco



Tobacco

Overview

According to the Department of Health, the prevalence of smoking has reduced in Ireland in recent years with fewer people smoking than they did ten years ago and those who continue to smoke, now smoking less. Reported figures indicate that the rate of non Irish duty paid cigarettes consumed in the country have also decreased from 22% in 2009 to 17% in 2014. Despite these reported reductions, illicit trade in tobacco continues to create a significant cost in terms of annual loss of revenue to the Exchequer. The impact goes beyond purely financial loss, posing threats to both compliant businesses and public health.

What is illicit trade in tobacco?

Illicit trade in tobacco deals with the production, importing, exporting, purchasing and sale or possession of tobacco failing to comply with legislation. There are three main classifications of illicit tobacco: contraband, counterfeiting and illicit whites.

The incentive to buy illicit tobacco continues to be driven by price and affordability and the incentive to supply by margins available to illicit traders.

Development - price

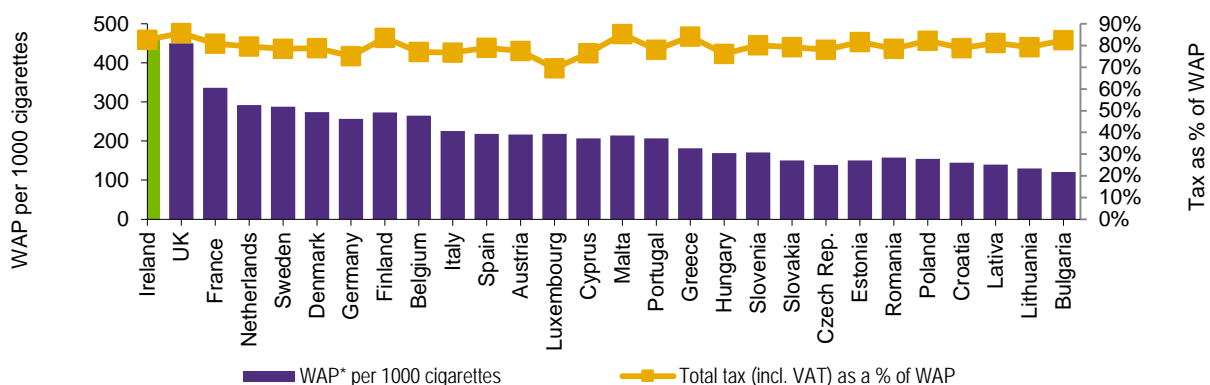
A key driver for the illicit trade in tobacco products is the level of excise duty. Criminals are attracted to the high profitability of this market as taxation policies across different jurisdictions give rise to opportunities for illegal traders to make profits by not paying domestic rates of duty.

From a demand perspective, increases in excise duties drive up the final price of cigarette products which in turn increase demand for cheaper products supplied by the illicit market.

In Budget 2016 the excise duty on a packet of 20 cigarettes was increased by 50 cent (including VAT) resulting in each 20 pack now costing €10.50 for the first time.

Prices in Ireland (and the UK) remain significantly more expensive than in other EU Member States. Successive increases in taxes on tobacco and VAT have resulted in cigarettes in Ireland being among the most expensive in the EU. Ireland with 83% of total tax (incl. VAT) as a percent of the Weighted Average Price (WAP), ranks fifth behind the UK (86%), Finland (84%), Greece (84%) and Malta (85%).

Figure 4.1 Excise Duty per 1000 cigarettes in the EU



* WAP = Weighted Average Price
 Source: "Excise Duty Tables Part III Manufactured Tobacco" European Commission

Development - legislation

Public Health (Standardised Packaging of Tobacco) Act 2015

On 10 March 2015, Ireland introduced The Public Health (Standardised Packaging of Tobacco) Act 2015.

The aim of the legislation is to remove the marketing ‘fashion element’ from smoking to discourage children and young people taking up the habit.

The new legislation bans all forms of branding such as trademarks and logos on packs of cigarettes, tobacco and cigars and introduces 65% health warnings on the packs. It is intended that these changes will begin to take effect from May 2016 and be fully in place by May 2017²⁴.

Concerns have been expressed by the tobacco industry and the international business community that the introduction of the plain packaging will have the effect of removing the protection of their brand and intellectual property making products easier to counterfeit.

The BASCAP, an initiative of the International Chamber of Commerce (ICC), supports these concerns stating that that standardised packaging “*would increase the prevalence of counterfeit goods in the market, reduce brand owners' ability to take action against such activity and undermine the ability of consumers to make informed purchasing decisions*”, thus making it easier to counterfeit a product and easier to mistake a counterfeit product as genuine.

Tax stamp

Revenue and An Garda Síochana claim that the new legislation on plain packaging will not have any significant impact on illicit trade for tobacco products.

Revenue have advised that “*the tax stamp is a key means for them to distinguish between legal and illegal products, irrespective of the way in which the cigarettes are packaged*”.

The new tax stamp was introduced on tobacco products from April 2015.

The Revised Tobacco Products Directive (2014/40/EU)

In May 2014 the Revised Tobacco Products Directive (2014/40/EU) was formally published by the EU. With an effective date of May 2016, it includes a requirement that EU member states “*must introduce a tracking and tracing system for tobacco products, based on a 'unique identifier'*”, a key security feature which will mostly likely be based on number codes “*placed on every packet*”²⁵.

“Ireland is an ending point for illegal tobacco products due to cigarette prices among the highest in the EU”.

Transcrime. European Outlook on the Illicit Trade in Tobacco



Cross-border issues with Northern Ireland

The price of tobacco is at similar high levels in Ireland, Northern Ireland and the UK. The incentive to supply cheaper illicit products in these markets is driven by margins available to illicit traders from smuggling products from cheaper jurisdictions to sell in these markets.

Driven by profits, it is reported that cigarette smuggling is one of the main sources of funding for former paramilitary groups in Northern Ireland and Ireland²⁶.

The open border

The open border between Ireland and Northern Ireland facilitates the smuggling of illegal tobacco products into Ireland. In addition to using Irish airports, smugglers use Irish ports as a back door for introducing the illegal product into Northern Ireland and the UK because it is more difficult to bring them through the Belfast port²⁷.

Cooperation between Organised Crime Groups (OCG)

In recent times, both jurisdictions are starting to see the presence of foreign OCGs as players in the market.

As well as working with foreign OCGs, close cross-border cooperation between the OCGs of Ireland and Northern Ireland is reported²⁹. According to Interpol, former paramilitary groups in Northern Ireland and Ireland are engaged in overseas trafficking of tobacco through containers, in addition to paying individuals to bring tobacco in from overseas in small quantities^{28, 30}.

Cross-border cooperation

The authorities in Ireland and Northern Ireland continue to work together to find ways to combat illicit trade activities with cooperation on both an informal and formal basis. The primary focus of the Cross-Border Tobacco Fraud Enforcement Group, a multi-agency special cross-border force, is to tackle this problem. They meet on a periodic basis throughout the year.

The BIPA report recommended that an all island approach be taken to tackle cross-border illicit trade and welcomed the development of this task force. Acknowledging the lack of resources for enforcement, one of the key recommendations coming out of the report was that the Cross-Border Enforcement Groups “*establish a permanent, full time task force dedicated to eliminate activities of organised crime gangs involved with cross-border illicit trade*”.

Table 4.1: Price differentials between the Northern Ireland and Ireland (2015)

Tobacco	Price ROI €	Price N.Irl €	Variance €	Total Tax ROI €	Total Tax NI€	Variance Total Tax €	Tax as % of price ROI €	Tax as % of price NI
Cigarettes (20)	10.00	12.52	(2.52)	7.87	9.26	(1.39)	78.7%	74.0%
Roll your own tobacco (25g)	11.40	12.95	(1.55)	8.96	8.42	0.54	78.6%	65.0%

Source: Revenue Commissioners price comparison survey, September 2015

Enforcement

The main bodies involved in the fight against the illicit trade in tobacco products are Revenue, An Garda Síochána and the Cross Border Tobacco Group. Cooperation takes place with other Revenue administrations and with the European Anti-Fraud Office (OLAF) in ongoing international programmes aimed at tackling illicit trade.

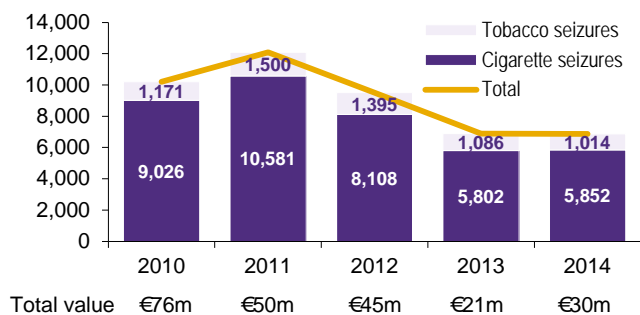
Seizures and convictions

The quantity of cigarettes seized in Ireland decreased between 2010 and 2014 as shown in Figure 4.2. However, Revenue's 2015 "Economics of Tobacco" report signals that such decreases may not provide a wholly useful indicator of illicit market trends as they can be "a function of the quality and intensity of enforcement activity or shifts in how cigarettes are smuggled".

Notwithstanding the general downwards trend, there have been some high profile seizures in the latter half of 2015:

- November: Over 681,000 smuggled cigarettes were seized in Rosslare Europort, representing a potential lost to the Exchequer of circa €285k;
- October: A total of ten million illegal cigarettes were seized in Slane, Co Meath representing a potential street value of €5.25 million and loss to the Exchequer of circa €4.2 million;

Figure 4.2: Number of excisable tobacco products seized between 2010 and 2014

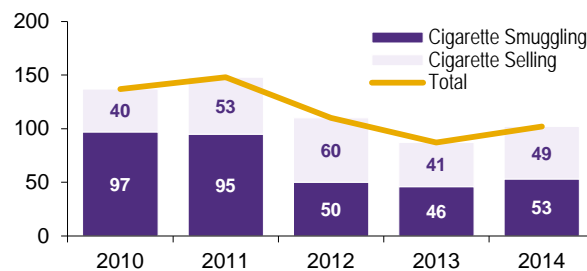


Source: Revenue Commissioners Annual report

- September: A total of 445,000 illegal cigarettes were seized in Cork, representing a potential street value of €225k and loss to the Exchequer of circa €180k; and
- August: A total of eight million illegal cigarettes were seized at Dublin port, representing a potential street value of over €4m and loss to the Exchequer of over €3.2m.

Convictions have also decreased between 2010 and 2014 yet the mix of criminals convicted for cigarette selling versus smuggling has changed with a higher percentage of convictions for selling in later years. This is highlighted in Figure 4.3.

Figure 4.3: Criminal convictions for cigarette smuggling and selling between 2010 and 2014



Source: Revenue Commissioners Annual report

Recommendations

The following recommendations have been put forward by Transcrime in relation to reducing illicit trade activities in tobacco products in Ireland:

- increased international cooperation and exchange of data with EU and non-EU law enforcement agencies to reduce tobacco flows into Ireland;
- strengthening of controls in the Irish ports and airports which are key entry points of illicit tobacco; and
- promoting security preventive measures for all persons engaged in the tobacco supply chain.

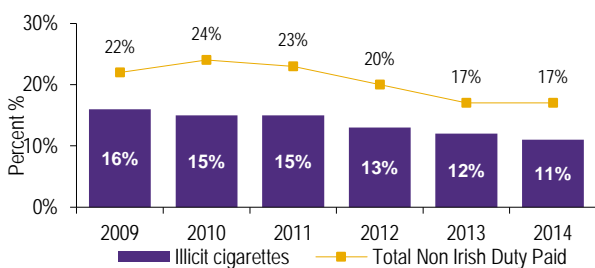
A further recommendation is to increase the penalty for these crimes. In Ireland there are very low penalties imposed for crimes relating to illicit trade in tobacco products, another factor which makes this an attractive trade for criminals.

Cost to the economy

It is estimated that around 12% of the global cigarette market is illicit. This is equivalent to 660 billion cigarettes each year and costs national governments more than US\$40bn a year in lost tax revenues³¹.

In Ireland it was reported that 11% of the cigarette market was from illicit trade in 2014, a reduction from 16% recorded in 2009.

Figure 4.4: Percent of non Irish duty paid cigarettes



Source: IPOS-MRBI annual survey carried out on behalf of the Revenue Commissioners and the HSE

Table 4.2: Estimated losses to Exchequer and industry (cigarettes) 2014

	2014
Excise receipts (€million)	881
Price	€9.60
Excise content as % of price	59.2%
Total sales (€million)	1,490

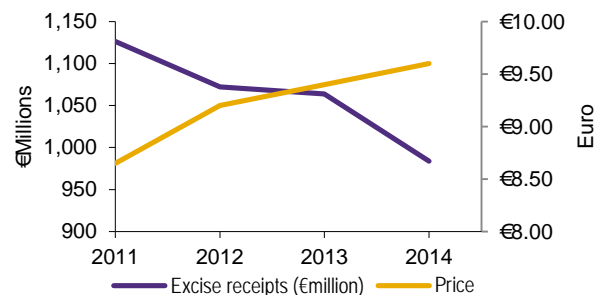
In 2014, non-Irish duty paid cigarettes accounted for 17% of the cigarette market in Ireland according to Revenue figures. This resulted in estimated losses of €253m to the industry and €197m to the Exchequer.

However, the MS Intelligence “empty pack” survey suggests that the real cost of non Irish duty paid cigarettes is much higher than Revenue estimate. Our previous reports also concluded that some estimates suggested that the overall consumption of illicit tobacco was higher.

Figure 4.5 illustrates that, in Ireland, as the price of a pack of cigarettes increased year on year, excise receipts have declined. Specifically, between 2011 and the end of 2014 the price of a 20 pack of cigarettes has risen from €8.65 to €9.60 while excise receipts declined from €1,057m to €881m. Total sales decreased by 13.8% during this period.

Factors why this may occur include potential rises in illicit trade that is undetected, cessation of smoking, and alternative products.

Figure 4.5: Excise receipts versus price



Source: Revenue Commissioners and Department of Finance

Source of estimates	Illicit		Non-Irish Duty Paid (NIDP)	
	Revenue	KMPG	Revenue	MS Intelligence
%	11%	15.9%	17%	24%
Estimated losses (€million)				
Loss to Industry	164	237	253	357
Loss to the Exchequer (Excise)	97	140	150	211
Loss to the Exchequer (VAT)	31	44	47	67
Total Loss to the Exchequer	127	184	197	278

Source: Source: IPOS-MRBI annual survey carried out on behalf of the Revenue Commissioners, KPMG Project Sun report, MS Intelligence Empty Pack Surveys and Grant Thornton analysis

Budget shortfalls

There has been a shortfall between the expected yield and actual yield on the excise receipts generated through budgetary measures over the last number of years. For example, in 2012 there was a 44 cents increase in the price of a 20 pack of cigarettes. This led to an expected annual additional yield of circa €38m yet a shortfall of circa €92m occurred.

Table 4.4 highlights continued shortfalls each year amounting to a cumulative budget shortfall of circa €303m for the period 2010 to 2014. The figures for 2015 are not yet available.

These continuous shortfalls alongside year-on-year tax increases highlight that raising taxes on tobacco does not guarantee additional generated tax yields. The current government appear to assume no changes in consumer behavior towards smoking when calculating tobacco tax yields. Future estimations of tax yields need to take into account other additional factors such as illicit trade, smoking trends and alternative options such as electronic cigarettes.

Table 4.4: Excise receipts – expected versus actual yield

Year	Previous years yield (millions)	Budgeted additional yield (millions)	Expected yield (millions)	Actual yield (millions)	Budget over/ (shortfall) (millions)
2010	1,216	-	1,216	1,160	(57)
2011	1,160	-	1,160	1,126	(34)
2012	1,126	38	1,164	1,072	(92)
2013	1,072	20	1,092	1,064	(28)
2014	1,064	12	1,076	984	(92)
2015	984	41	1,025	not available	not available

Source: Official budget statements and Grant Thornton analysis

Impact on consumption

It is important to note that the Government's stance on raising the price of cigarettes is not to generate additional excise receipts but an attempt to try and deter more people, especially youths, from smoking. This is supported by the WHO which claims that a 10% increase in the price of a pack of cigarettes decreases smoking by 4% in high income countries which include Ireland. Over the years, continuous annual increases in taxes on a 20 pack of cigarettes can be aligned with the decrease in the number of smokers in Ireland during the same period.

While recent Eurobarometer and Health Service Executive (HSE) data indicate that smoking prevalence has reduced substantially in recent years, it is important to note that customers may respond to tobacco tax increases by finding cheaper alternative ways to source the product. It is difficult to fully rely on illicit trade figures as tobacco smugglers are constantly becoming more innovative in order to avoid detection. While the Revenue-reported percentage of non Irish duty paid cigarettes for 2014 was 17%, the MS Intelligence “empty pack” survey claimed that the incidence is significantly higher with Irish duty not being paid on as many as 24% of consumed cigarettes.

Future impact on tax increases

It is often assumed that there is a positive correlation between the rate of taxation and tax revenue.

In their pre-election manifesto, Fine Gael pledged to “*increase the excise duty on a pack of 20 cigarettes by 45 cent per year, with a pro-rata increase on other tobacco products*”. The party expects such an increase to yield an extra €349m in revenue over five years, according to their long term economic plan. Similarly, Labour's manifesto commits the party to increasing tobacco tax “*each year to yield approximately €260m after five years*”.

However, Revenue's 2011 “Economics of Tobacco” report outlines how these projections do not take into account a “laffer curve type effect” in the cigarette market in Ireland. This suggests that beyond a certain optimum point, tax rises may actually decrease revenue. Recent trends in Ireland, as outlined in Figure 4.5, suggest that Ireland's tax rate is beyond than this “tipping point” and future revenue gains as a result of increasing tobacco taxes are not guaranteed.

Even if the primary motivation of tobacco tax increases is to disincentivise smoking, it is important to note that demand for tobacco products is price inelastic. This means that even as the price of tobacco increases the decline in the number of smokers will not be 100% correlative due to the fact that certain smokers are addicted to tobacco products and, traditionally, there have been no close substitutes. These smokers will purchase the product regardless of the price or, as previously described, find cheaper alternatives, for example via illicit trade.

If the government continues to increase the tax on cigarettes it can be assumed that the future impact will be a further decrease of tax revenue, a decline in the number of smokers, and a strengthening of illicit trade.

This is supported by the 2011 “Economics of Tobacco” report which finds:

- further tax (price) rises will reduce smoking somewhat but they will also greatly encourage more untaxed consumption;
- increasing the taxation of cigarettes in Ireland no longer carries the combined benefits of better public health and higher revenue for the public finances that would have arisen from such increases in the past;
- at the very least, these benefits are severely weakened by the substitution of untaxed for taxed consumption; and
- this suggests that taxation increases are no longer the optimum tool for reducing smoking in Ireland.

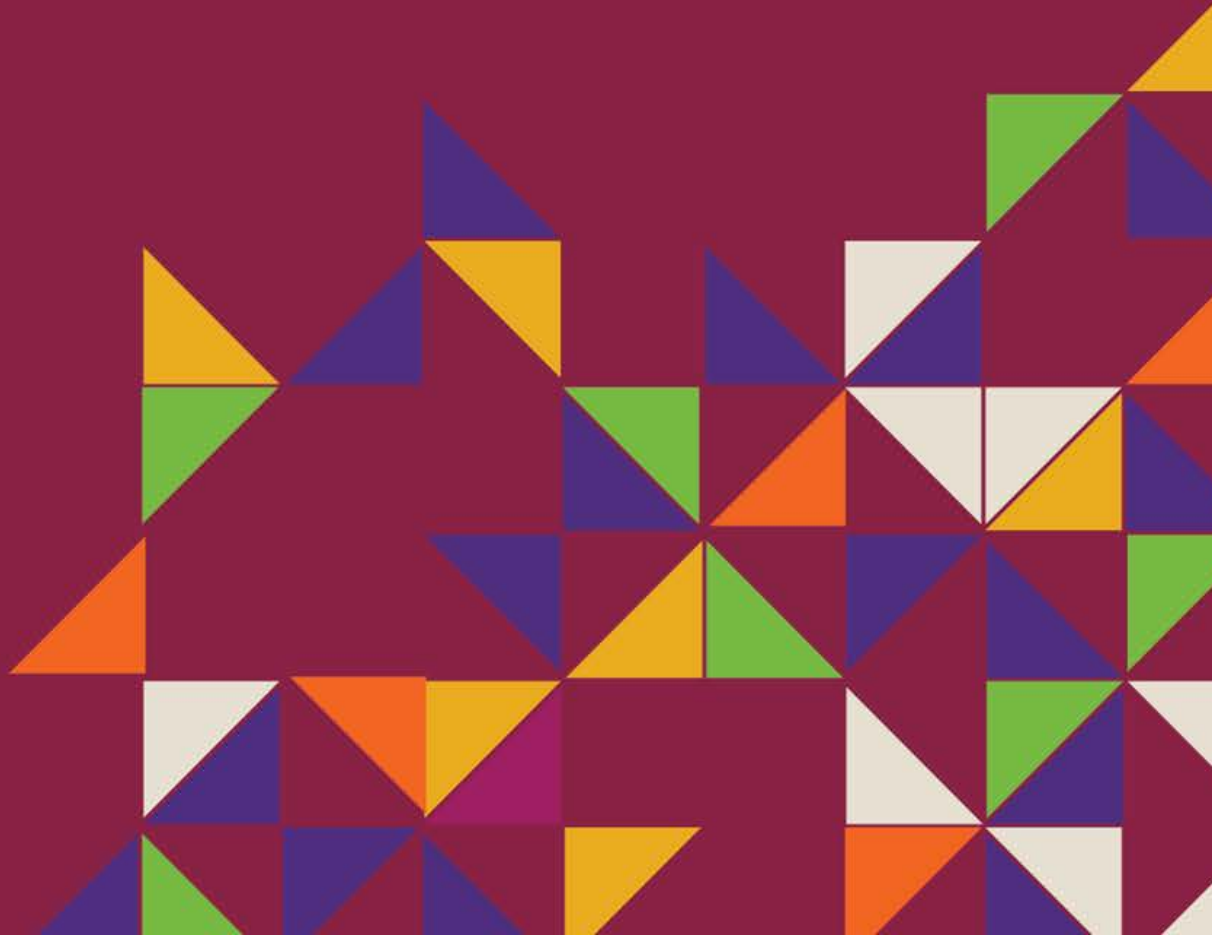
Increasing tax is not the only solution to reducing smoking rates in Ireland.

Other alternatives which can be just as effective include:

- health campaigns highlighting the dangers of smoking;
- continuing to evolve the ban on smoking in many public areas; and
- campaigns and new products to help people to give up smoking.



Pharmaceuticals counterfeiting



Pharmaceuticals counterfeiting

“Spurious, falsely-labelled, falsified, counterfeit medicines are medicines that are deliberately and fraudulently mis-labelled with respect to identity and/or source”. World Health Organisation

Ireland plays a key role in the pharmaceutical industry, with nine of the world’s top ten pharmaceutical companies having a significant presence here. Ireland is also Europe’s largest net exporter of medicines and the eight largest producer of pharmaceuticals in the EU, with €55bn of exports on an annual basis³². Given the scale of the pharmaceutical industry based here, the counterfeiting of pharmaceutical products continues to be an important issue for Ireland.

What is illicit trade in pharmaceuticals?

Illicit trade in pharmaceuticals relates to the sale of falsified or counterfeit medicines. A falsified medicine is any medical product with a false representation of its identity, its source, or its history. The following are characteristics of falsified/counterfeit medicines:

- can be authentic, branded and generic medicines;
- contain correct or incorrect ingredients;
- packaging or labelling may be falsified;
- supplied without valid prescription; and
- contain insufficient, too much, or no active ingredients.

Key driver - price

Price remains a key driver for the illicit trade in pharmaceutical products. Even with the price reductions in recent years, as a result of the introduction of generic medicines, representatives from users of medicines maintain that the price of medicines remain higher in Ireland than other Europe countries.

From a patient’s perspective, medicines can be seen to be too high a cost, especially when they accompany other treatments which may also need to be funded. As counterfeit medicines can be made cheaply and sold for 50% of the cost of the real medicine, they are attractive for those looking for cheaper options³³.

Facilitator - e-commerce

The spread of e-commerce has facilitated the purchase of illicit medicines in the market. For example:














- the WHO reports that in over 50% of cases, pharmaceuticals purchased over the internet from websites which conceal their identity are counterfeit; and
- medicines are purchased online for reasons such as:
 - cheaper prices;
 - access to drugs not readily available in Ireland;
 - maintenance of anonymity and privacy to access medicines without being questioned; and
 - no requirement for prescriptions/self medication.

Social media has also assisted in facilitating the purchase of falsified medicines in the market as sellers turn to these websites to advertise their products.

“50 per cent of the medicine sold by unregulated online retailers is estimated to be unreliable and potentially harmful”.

Former Minister for Health Leo Varadkar – June 2015

Key facts and statistics on counterfeit pharmaceuticals

-  Approximately 60 different Pfizer medicines and products were being counterfeited around the world in 2014.
-  The prescription drug market was worth up to \$989 billion world wide in 2013.
-  Most counterfeit medicines have been manufactured in China or India.
-  10,603 websites selling counterfeit medicines were shut down in 2014.
-  Only 237 people were arrested worldwide in 2014 for selling counterfeit medicines.
-  WHO estimates that between 1% and 10% of medicines sold around the world are counterfeits and that the figure may be as high as 50% in some countries.
-  Chapstick is one of the leading counterfeit items.
-  More than 30% of counterfeit drugs available today do not contain any active drugs.
-  About 85% of the world pharmaceutical market is in the developed world.
-  WHO estimates that 16% of counterfeit medicines include the wrong ingredients.
-  WHO reports that “in over 50% of cases, medicines purchased over the Internet from illegal sites that conceal their physical address have been found to be counterfeit”.
-  The value of the international counterfeit medicines market is \$200b annually.
-  An estimated 10-30% of medicines sold in developing countries are counterfeit.

Source: HealthResearchFunding.Org (December 2014), IMS Health WHO

Developments - legislation

In Ireland, the supply of prescription medicines by online retailers is prohibited. Pharmacies and retailers are only allowed to supply non-prescription medicines on the internet.

Steps have been taken at EU level to try to prevent falsified and counterfeit medicines from entering the legitimate supply chain.

EU logo

- counterfeit goods, particularly goods that impact the health and safety of the consumer, have become an enforcement priority for EU member states;
- in response, the EU has introduced a common logo for legally operating online pharmacies/medicine retailers in the EU Member States;
- as of 1 July 2015, all online pharmacies or retailers legally operating in the EU are required to display the logo;
- the logo will be linked to a public register which can be checked via the web page; and
- in Ireland, the supply of prescription medicines by online retailers is prohibited. Pharmacies and retailers are only allowed to supply non-prescription medicines on the internet.

Serialised track and trace

- serialised track and trace is another measure introduced by the EU False Medicines Directive to fight against falsified medicines. This involves the introduction of a unique and verifiable serial number for every saleable unit;
- the serial number uses Radio Frequency Identification (RFID) technology or 2D barcodes;
- it is intended that the serial number will allow for the verification of packages at the point of dispensing. In addition, any member of the supply chain will also be able to verify the origin of a package at any point; and
- serialisation is also being introduced on a global basis and each jurisdiction has its own timeframe for implementation. In the EU, 100% of prescription drugs must comply with the provisions of the Directive by Q1 2018.

Enforcement

Investigations and seizures

In 2014, there were 46 joint controlled delivery operations involving Revenue Customs Service and An Garda Síochána, and/or the Irish Medicines Board. These authorities also participated in several international operations including:

- targeting trade in illicit/counterfeit medicines and internet pharmacies;
- a joint EU regional maritime customs operation;
- an EU wide operation focusing on drugs and synthetic drugs;
- the seizure of over 142,000 illegal prescription medicines worth €430,000 in Ireland in June 2015 as part of a global Interpol investigation called Operation Pangea VIII; and
- the detention of a total of 20,709,037 illicit and counterfeit medicines with a value of €72m.

These investigations involved 236 agencies across 115 countries. Irish agencies included the Health Products Regulatory Authority (HPRA), An Garda Síochána and Customs.

Figure 5.1: Operation Pangea seizures – Ireland

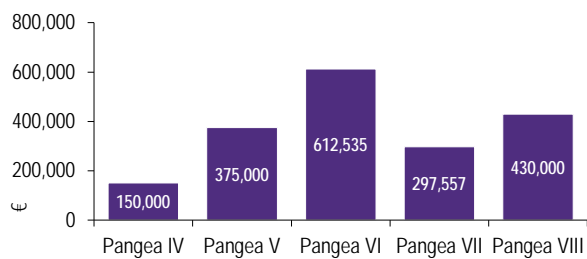


Table 5.1: Operation Pangea global results 2011 to 2015

	Pangea IV	Pangea V	Pangea VI	Pangea VII	Pangea VIII
Year	2011	2012	2013	2014	2015
Participating countries	81	100	99	113	115
Illegal websites shut down	13,500	18,000	13,700	11,800	2,410
Global value	€m	€m	€31m	€22m	€72m

Source: Interpol and Grant Thornton analysis

Cross-border issues with Northern Ireland

A key driver for cross-border activity is the price differential between Northern Ireland and Ireland in the price of medicines. This gap has narrowed in recent times as a result of reduced prices, following the introduction of reference pricing and the strengthening of the UK sterling against the Euro, which have made it less economical to travel to purchase certain medicines.

However, representatives from users of medicines maintain that pharmaceutical prices remain higher in Ireland. Cross-border travel therefore continues to be incentivised by lower costs along with the avoidance of the GP fee³⁴. There also remains a market for prescription medicines in Ireland that can be purchased without prescription in Northern Ireland.

Northern Ireland is used as a convenient address to bypass regulatory controls in Ireland for the purposes of transiting abortifacients³⁵. Furthermore, it is reported that the postal system in the UK is increasingly being used by illegal traders to disguise the source of pharmaceuticals. Items coming from China, India etc. use the UK as a convenient postal address as it draws less attention to the illicit items than if their true source was stated. There are no significant trade implications of such practices as the medicines are not originating in Northern Ireland and for the most part they are not displacing legitimate trade in Ireland³⁶.

There are however issues around certain medicines being diverted from the legitimate trade. This is currently under investigation in Ireland and the UK. In particular, there are issues with regards to the illicit trade of sedatives. This relates to items which are mostly legitimate, but are illicitly traded by organised crime gangs through channels such as street dealing.



Cost to the economy

It is difficult to determine the costs of the illicit trade of pharmaceuticals on industry and the Exchequer. The information available makes compiling statistics challenging.

Illicit trade in medicines in Ireland is different from some of the other areas discussed in this report. For the most part the illicit trade in medicines does not displace legitimate trade. This is because most of the illicit market which we see in Ireland does not qualify for prescription medicine supply and would not be available for purchase³⁷.

It does however impact the manufacturers who operate and export out of Ireland. WHO estimates that between 1% and 10% of medicines sold around the world are counterfeits and may be as high as 50% in some countries. As illustrated in Table 5.2, from an international perspective the figures are substantial. According to UN Comtrade statistics, the Irish share in global pharmaceutical exports is 5.4%. This is down from 7.7% in 2011.

When we apply reported losses to the global pharmaceutical industry to the Irish market the losses suffered by the Exchequer and the industry are significant. Recent estimates indicate that Irish exporters have potentially suffered losses in the region of €3bn in 2014 and that losses to the Exchequer by way of corporation tax receipts are in the region of €45m. As with other estimates, the information available is limited and in reality the losses are likely to be higher.

Industry opinion

The introduction of the EU logo will have a positive impact, protecting the health and safety of consumers by ensuring that medicines are purchased from a legitimate pharmacy.

More efforts are needed to increase public awareness on the health care issues which can result from the purchase of falsified medicines online.

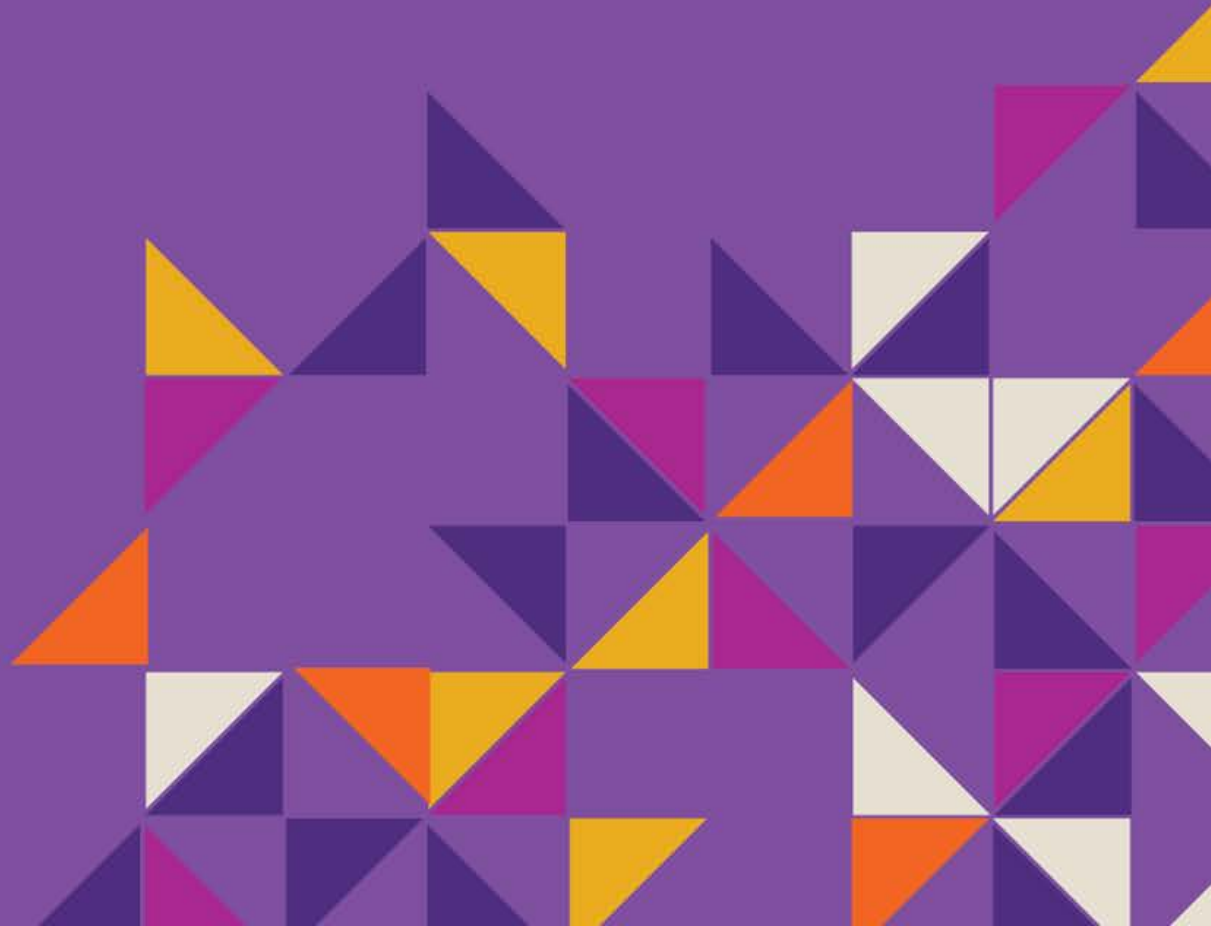
In addition, public education is needed to inform unsuspecting consumers about what to look out for when purchasing what they expect to be a genuine product.

Table 5.2: Estimated value of illicit trade in pharmaceuticals

	IMS Institute 2014		EFPIA 2013	
Estimated value of global pharmaceutical market:	\$1,027bn		\$870bn	
- US\$ billions	\$1,027bn		\$870bn	
- € billions	€884bn		€655bn	
Illicit trade range	Low - 5%	High - 8%	Low - 5%	High - 8%
Value of global Illicit trade (€billion)	€44.2bn	€71.7bn	€32.8bn	€52.4bn
Irish share of global exports in 2014	5.4%		5.4%	
Estimated loss Irish exporters (€billion)	€2.4bn	€3.8bn	€1.8bn	€2.8bn
Estimated loss to the Exchequer (€million)	€36.27m	€58.04m	€26.89m	€43.02m

Source: Grant Thornton analysis

Digital piracy





Digital piracy


The Internet has become the principle platform for the delivery of digital content such as movies, television, music, books, news and software. The global reach of the internet means that digital content can be delivered anywhere in the world, in an instant and for a significant reduction in cost when compared to physical content products. The internet, as a new way of content delivery, has also facilitated the spread and increase in digital piracy, a topic which remains a major issue for both the global and Irish markets.


The digitalisation of products


The digitalisation of products has had a profound effect on how we do business today, particularly in the IP intensive sectors. As technology continues to evolve, improve and expand, new models for how we do business have also evolved in the following ways:


- Marginal cost of reproduction** 

The internet is used as new way to deliver content, for example iTunes.
Delivery via the internet or local area networks is flexible and also significantly reduces the cost of acquisition.
- Digital delivery** 

Once created an item can be reproduced with relatively little cost or effort.
- Unlimited geographic market scope** 

The use of the internet facilitates products being instantly delivered all over the world.
- Portability of content** 

The growing use of mobile devices such as smartphones, tablets and ebook readers has improved the portability of content.
- Life span** 

The lifespan and durability of products is significantly increased.
- New revenue models** 

There are new ways to generate revenue, such as advertising-based models, pay per view and subscription-based models, for example Netflix and Spotify.

“The rapid development of the Internet implies that more people than ever before have access to practically any type of news or data. However, this technological progress also facilitates digital piracy, as users employ various web based workarounds and applications to distribute and exchange large amounts of pirated digital products instantaneously around the world” Copyright in the Digital Era: Country Studies, OECD



What is digital piracy?

Digital piracy is a term used to describe illicit activities linked to a range of infringements on IPR. It includes audio-visual piracy, software piracy and the theft of other electronically transmittable IP.

Key drivers

- demand is driven by convenience, access to products and price. The global reach of the internet means that digital content can be delivered anywhere in the world and in an instant, for a significant reduction in price when compared to physical content products;
- research suggests that the problem people have is not solely about the price of the content; rather it relates to limitation in accessing the content. Instant access to pirated products make them more attractive when the alternative is to wait for legitimate items to become available. In addition, it is thought that region-locking content drives piracy as consumers look elsewhere for access;
- digital piracy is perceived to be a victimless crime as little to no financial gain arises from the distribution of digitally pirated products online;
- due to the high numbers engaging in illegal downloading it is very difficult and uneconomical to pursue individual offenders;
- existing legislation currently does not provide appropriate remedies for copyright holders in respect of on-line infringements; and
- the drivers of digital piracy are not always the same as the other illicit activities discussed in this report. While profit is certainly a driver, with revenues generated from advertising or from premium subscription fees, digital piracy is also driven by non-market factors, such as suppliers gaining recognition within a peer group, reciprocating free access to other users, or sharing products online. This behaviour can be sustained because the marginal cost of reproduction and delivery of digital content is zero, or close to zero³⁸.

Legislation

Ireland's main copyright legislation is the Copyright and Related Rights Act 2000.

The legislation is over 15 years old and is outdated considering the technological developments and changes in the online environment which have arisen since then³⁹.

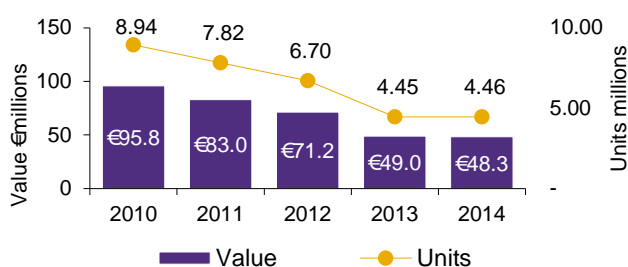
In October 2013, a report "modernising copyright" was issued by the Copyright Review Committee. The report recommended a series of amendments to the Irish Copyright and Related Rights Act, 2000, including a broader "fair use" provision. With regards to digital piracy, the recommendations, when fully brought into law, will provide the legal system with greater ability to respond to the changing needs of the digital/online environment.



Key developments - film and television

The landscape of retailers offering home entertainment has changed in recent years. This is noticeable in particular with the decline in the video market from 2006 to 2014.

Figure 6.1: Irish retail video market 2010 to 2014



Source: Irish independent film distribution company

The industry is of the view that there are various contributing factors to this change, the major contributor and the greatest cause of concern to the industry being *“the rise of illegal digital viewing which is now endemic”*⁴⁰.

With regards to film, the majority of the illegal content starts its life in the cinema with the illegal recording and broadcasting of the content online. This mainly impacts the larger production houses such as Warner Brothers, MGM etc. In Ireland, the industry is concerned that digital piracy is having a devastating impact on the independent film-maker, in addition to retailers. They are totally dependent on local distributors in all countries to take risk and invest in the making of a film before it is made. *“As a result independent film makers have been virtually wiped out”*⁴¹.

Region-locking content forcing piracy?

Reinforcing the argument that digital piracy is often driven by issues around availability and access, Hollywood director, Lexi Alexander has commented that she thinks piracy is necessary because of country content restrictions *“As an expat household, with three paid Amazon Prime memberships for three different countries, a paid Netflix membership, a paid ACORN membership, a ridiculously high DISH [pay TV] bill and an Apple TV box, we still can't watch most programs from back home, even though we're willing to pay good money for it.”*

Cinema release window

A key motivation for people to illegally download movies is the long gap between a film being available in the cinema and through other channels. On average this is around 120 days, however it can extend to longer periods depending on the country. In addition, movie cinema releases are often at different times of the year in different countries.

For example films are released in the USA before they are released in Ireland. In a move to change this the production houses are considering shorter release windows. In July 2015, Paramount Pictures struck a deal with two major cinema chains to make new movies available to watch via home entertainment systems two weeks after they leave most cinemas. The new arrangement will begin with two films and is considered a step in the right direction.

Irish illegal downloading trends

Research carried out in November and December of 2014 by Ignite Research on behalf of Core Media reports that over 36,000 people in Ireland illegally download TV and video content every day. The report also noted that 31% of people are illegally downloading less material than they were twelve months ago. The reason for the decrease is the improved access to material by way streaming channels such as Amazon Prime and Netflix at relatively low cost.

“Distributors are not able to take the risks they used to. What this means to the consumer is not that some producers don't get rich, it means the product doesn't get made”. Jean Prewitt, Head of the Independent Film and Television Alliance



Key developments - music

Internet based approaches have changed the way that most musicians market themselves and engage with their audience. They have harnessed the power of the internet as a way to communicate in a more direct, frequent and less expensive way with their fans. As a result, music subscription services have seen the number of paying users increase in recent years. The International Federation of the Phonographic Industry (IFPI) estimate the following in relation to music subscriptions in 2014:

- more than 41 million people worldwide now pay for a music subscription, up from just eight million in 2010 (2013: 28 million); and
- global revenues from subscription and advertising-supported streams now account for 32% of digital revenues, up from 14% in 2011.

With this increase in music subscriptions there is also the issue of digital piracy. The IFPI estimate that 20% of fixed-line internet users worldwide regularly access services offering copyright infringing music.

However, the research would indicate that the introduction of streaming services such as Spotify reduces the incidence of piracy. This strengthens the argument that often digital piracy is driven by issues around availability and instant access and not mainly on price.

“Music piracy is on the decline in Ireland thanks to growing use of streaming sites such as Spotify and Deezer”.



IMRO Victor Finn, chief executive of the Irish Music Rights Organisation (IMRO) in conversation with Siliconrepublic.com



Enforcement

Litigation is the vehicle typically used to curb illegal downloading but its success to date has been limited. The legislation is dated and due to the high numbers engaging in illegal downloading it is very difficult and uneconomical to pursue offenders. In response, the affected industries have attempted to stop the supply by pursuing websites that facilitate the downloading of illegal content and forcing them to shut down, or restricting access to them through site blocking.

Actions taken		
Search engines	<ul style="list-style-type: none"> search engines are a significant driver of traffic to unlicensed websites; and they play a major role in influencing the decisions about how and where to obtain content. 	<ul style="list-style-type: none"> in October 2014, Google announced that it would be taking action to demote sites for which a large number of valid take down notices from copyrights holders were received. This forced pirate sites that were subject to a high number of these notices to move down the search rankings. However, this has not had the desired effect, as very often the ranking is replaced by other previously high ranking pirate sites; and the affected industries are calling for further action to ensure that consumers are directed to legitimate and not to pirate sites⁴².
Website blocking	<ul style="list-style-type: none"> this is action taken by ISPs to block access to copyright infringing websites; and it is becoming an increasing accepted way of effectively helping to tackle digital piracy. 	<ul style="list-style-type: none"> in March 2014, the EU Court of Justice ruled that the blocking of copyright infringing sites is compatible with EU law. Courts in 11 EU countries have ordered Internet Service Providers (ISPs) to block users' access to infringing websites. The IFPI Digital Music Report 2015 comments that <i>"since the Pirate Bay and numerous other sites have been blocked in the UK there has been a 45 per cent decline (from 20.4m in April 2012 to 11.2m in April 2014) in visitors from the UK to all BitTorrent sites, whether blocked by ISPs or not"</i>; and in March 2015, the High Court in Ireland ordered UPC to introduce a 'three strikes' anti-piracy policy internet policy. The ruling means that any UPC customer caught downloading pirated music or movies is set to be disconnected after two warnings and a further court process.
Advertising on pirate sites	<ul style="list-style-type: none"> major brands advertise on pirate websites, generating revenues for the pirate site owners. 	<ul style="list-style-type: none"> in July 2014, the European Commission announced that its EU action plan on the enforcement of intellectual property rights, among others, would include work streams with the objective of reducing the profits of commercial scale IP infringements in the online environment, involving advertising service providers and payment services. In addition, a number of countries including the US, UK, Spain, France and others are having discussions on this problem; and it is reported that the advertising industry is yet to take effective action and major brands continue to advertise on pirate sites.
Illegal cinema recordings	<ul style="list-style-type: none"> illegal recordings of films in the cinema are subsequently broadcasted on pirated sites. 	<ul style="list-style-type: none"> in Britain, anti-piracy teams have managed to dramatically reduce the number of cinema illegal recordings <i>"since they began training cinema staff who, armed in military-style goggles, scan theatres for recorders"</i>⁴³.
Mobile device apps	<ul style="list-style-type: none"> mobile device applications (apps) facilitate access to content through through downloading, streaming, stream ripping, and search. 	<ul style="list-style-type: none"> apps are most frequently downloaded from the large app stores operated by Google and Apple; and it is reported that, following requests by copyrights holders, both companies have taken some steps to remove apps that facilitate piracy. More effective action is needed as many of these apps, thought have been removed, remain available or reappear.

Loss to the economy

In terms of digital costs to the Irish economy, we estimate that in total:

- over 500 jobs were lost by 2015;
- retailers suffered losses of circa €320m in revenues; and
- the loss to the Exchequer in VAT receipts was as much as €71m as a result of digital piracy⁴⁴.

In 2014, it is estimated that almost 30% of people in the UK were watching movies illegally online or buying counterfeit DVDs. This translates to a cost to the industry of £500m a year⁴⁵.

On a positive note, the shift to the digitisation of products has seen companies such as Spotify and YouTube increase their activities and therefore increase workforce numbers. It could be argued that this has a positive impact in negating the effect of jobs lost in this sector.

Figure 6.2: Business sectors impacted by digital piracy



Industry opinion

The main issues arising from our research and consultation with industry players for policy makers to consider are as follows:

Education and awareness

More public education and consumer awareness campaigns are needed to educate users:

- that digital piracy, in addition to being illegal, is also unethical; and
- to help understand what is legal and illegal.

Access to content

Increased access to content by way of shorter release windows by the industry as a whole is needed.

Region-locking should be reconsidered to make content available globally and available in all areas at the same time.

Legislation

Existing legislation is outdated and not able to deal adequately with the rapid technological developments that facilitate digital piracy. There is a requirement for improving the speed at which it responds to copyright infringement.

Enforcement

Legal action against pirate websites and action against individuals infringing copyright are positive actions and bring some results.

Multi party cooperation

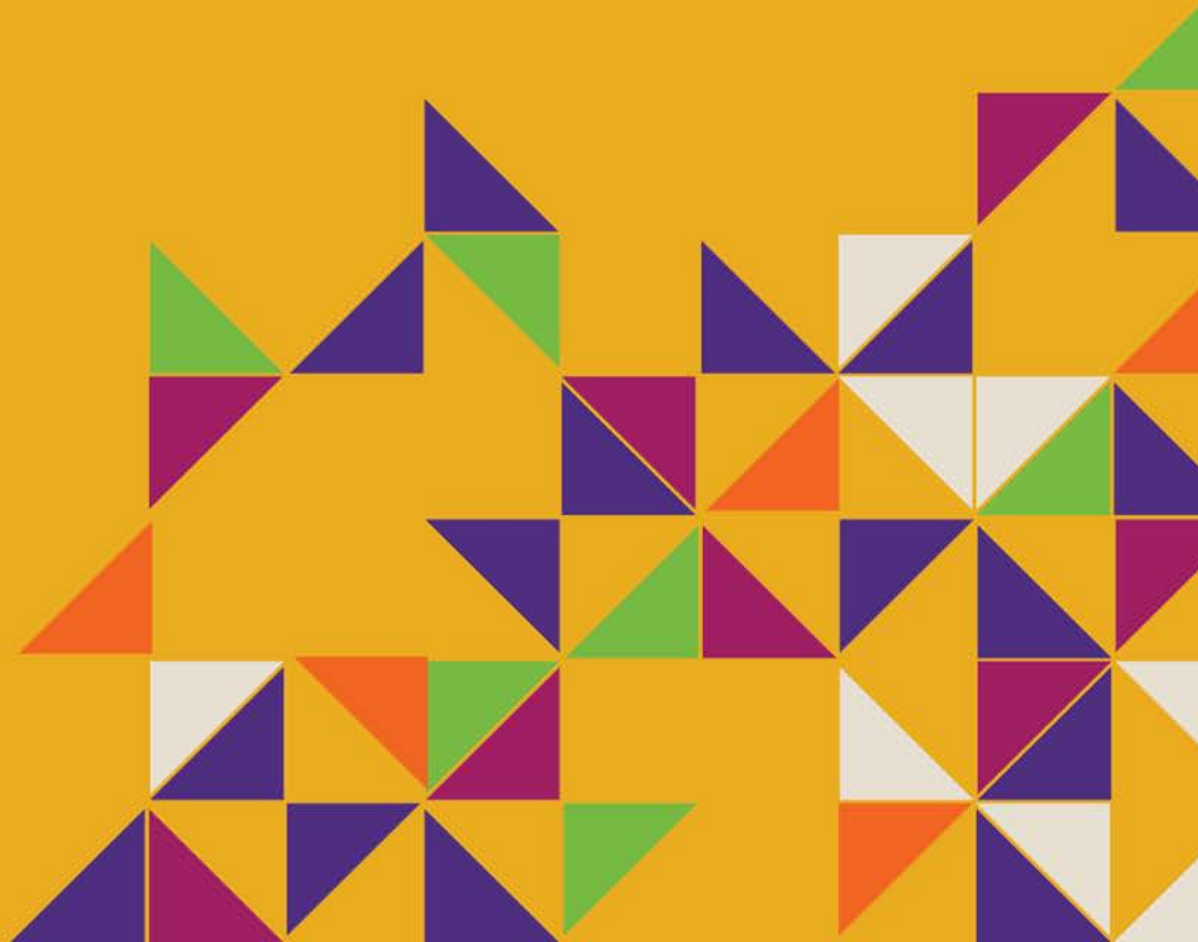
Digital piracy is global in nature with a very large number of actors involved in different jurisdictions. Tackling the problem therefore requires international cooperation between governments, enforcement agencies, the industry and consumers if they are to identify and take down the web sites involved in this activity.

Furthermore internet intermediaries need to take responsible action in order to help, for example by removing the advertising, a main revenue stream, from the pirate sites.

“The erosion of IP will have an increasingly large impact on the global economies and economies in Europe. It's important that we try to educate people to behave like responsible citizens and to be honest and understand why copyright matters”. Gareth Neame, executive producer of Downton Abbey



Other product counterfeiting



Other product counterfeiting

“Counterfeiting is the practice of manufacturing, importing/exporting, distributing, selling or otherwise dealing in goods, often of inferior quality, under a trademark that is identical to or substantially indistinguishable from a registered trademark, without the approval or oversight of the registered trademark owner”. The International Trademark Association



When we think of counterfeit goods, the words 'fake goods' or 'knock-offs' come to mind. In addition, counterfeit goods are often re-labelled or repackaged to make them appear like the genuine product.

The public perception of counterfeit good is ambiguous, as it is often seen as a victimless crime, yet this is not the case. It is an infringement of intellectual property rights of legitimate businesses. In addition, public safety is at risk as counterfeit products such as medicines, alcohol, electrical goods and toys can cause serious harm.

The top categories of goods most commonly detained at EU external borders are sports shoes, clothing and bags, wallets and purses⁴⁶. There is an increasing range of every day goods being counterfeited today, such as:

- tobacco;
- alcohol;
- medicines;
- food and beverages;
- batteries;
- phone chargers;
- clothing, bags and shoes;
- cosmetic and personal care products;
- electronic goods;
- household products;
- pesticides; and
- automotive mechanical products.

As a result of better technology, the counterfeit trade is growing rapidly, increasing in all areas of the supply chain from manufacturing, distribution, ordering and purchasing. According to Europol:

“The exact scale of the counterfeiting business is not known, however it is probably fair to assume that the reality exceeds all estimates and predictions”.

Given the scale of this activity, counterfeit goods, especially those that affect the health and safety of consumers, have become an enforcement priority in Ireland and Europe.

The counterfeit market

It is now estimated that the global total value of counterfeit and pirated products will reach USD \$1.77tr by 2015⁴⁷.

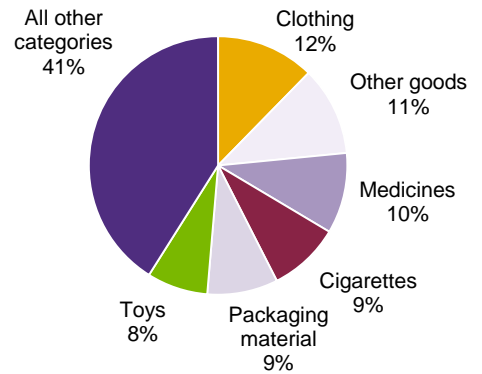
Key drivers

- high profit margins:
 - profits made are based on brand value: high-brand products generate more lucrative returns so items in markets with high demand are normally chosen to counterfeit; and
 - lower production costs: there is no quality assurance or health and safety standards in the production of counterfeit products, resulting in lower production costs.
- consumers are easy to deceive: the products and packaging are of such a high quality that consumers may think the product is legitimate; and
- consumer demand for cheaper priced products.

Methods used

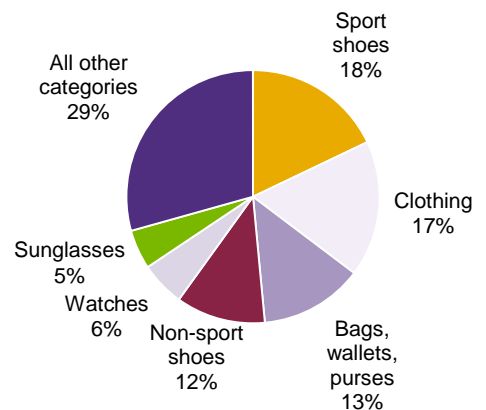
- abuse of weaknesses in infrastructure and supply chains using tactics, including:
 - the corruption of brokers between producers and distributors who can earn more with counterfeits; and
 - the encouragement of factory overruns, facilitated by the lack of factory inspections. This is accompanied by the falsification of documents, counterfeit trademark re-labeling, repackaging of products and the abuse of certification labels such as the ‘organic’ designation⁴⁸.
- evolving technologies offering more sophisticated and also cheaper ways to produce products:
 - the growth of 3D printing has made it possible for counterfeiters to be up and running at very little cost. It facilitates production as you go and in smaller batches thus reducing storage requirements. It also reduces the requirements for a factory, making tracking of the illegal traders more difficult.
- distribution channels that are easy to infiltrate.

Figure 7.1: Top categories seized at the EU border (2013) by product



Source: Report on EU customs enforcement of intellectual property rights, European Commission

Figure 7.2: Top categories seized at the EU border (2013) by articles



Source: Report on EU customs enforcement of intellectual property rights, European Commission


“The advent and subsequent rapid development of the Internet has raised the problem to heightened levels as counterfeiters find simplified means and additional channels in cyberspace to promote and sell counterfeit products to consumers”. The International Trademark Association



Facilitator – the Internet



The sale of counterfeit goods is a significant issue for consumers, industry and governments alike. Counterfeit goods continue to be widely available in both Northern Ireland and Ireland. The locations for point of sale have traditionally been street markets, car boot sales, door to door, at work and from homes⁴⁹. They are increasingly being sold online with the internet acting as a major facilitator for the sale and distribution of counterfeit goods. The ways in which this is facilitated are outlined below:

- Multi-jurisdiction  The internet is wide reaching and functions across multi-jurisdictions.
- Convenient  Websites are open 24/7 with items delivered to directly to customers homes.
- Payment processors  Counterfeit items can be purchased using credit cards, PayPal, Bitcoin, postal orders and cash.
- Social media  The use of Facebook and other social media sites to advertise and trade in counterfeit goods has increased significantly over the last number of years.
- Anonymous character  Criminal gangs can remain anonymous and difficult to track through the use of false identities to register domain names and proxy servers across multiple jurisdictions.
Websites can be set up and taken down overnight without losing their customer base.
- Quality of counterfeit websites  Some replicated website shops are of such quality that they rival, and in some cases are better than, those of the legitimate business.
- Advertising revenues  Revenues can be generated from both the sale of goods and from advertising.
- Spam  Spam is an easy, cheap and anonymous way to advertise online goods. This involves the targeting of consumers through spam emails with links to counterfeit websites.

Key developments - legislation

EU trademark reform

Businesses protect the intellectual property of the goods they produce by way of trademarks. A trademark is a monopoly right that protects any word, symbol (logos and package design) or device which distinguishes goods and services from another⁵⁰. There are two types of trademark: a national trademark and a community trademark.

On 27 March 2013, the European Commission presented a package of initiatives to make trademark registration systems across the EU “cheaper, quicker, more reliable and predictable”. The proposed package contained three initiatives:

1. Recast of the 1989 Directive (now codified as 2008/95/EC) approximating the laws of the Member States relating to trademarks (The Directive);
2. Revision of the 1994 Regulation (now codified as 207/2009/EC) on the Community trademark (The Regulation); and
3. Revision of the 1995 Commission Regulation (2869/95) on the fees payable to OHIM (The Fee Regulation).

One of the advantages of the reform is the introduction of more effective trademark protection against counterfeits which provide trademark owners with a better right to prevent the importation of counterfeit goods into the EU.









Trademark infringement - website blocking orders

A recent example of a website blocking order being actioned was from The Richemont Group, which owns several of the world’s leading luxury brands, including Cartier, Mont Blanc and International Watch Company (IWC). They applied to the English High Court for orders requiring the UK’s main ISPs to block access to six websites which had been identified as advertising and selling counterfeit Cartier, Mont Blanc or IWC goods.

Similar to copyright infringement cases, the blocking of which is compatible with EU law, there are ‘threshold conditions’ which must be met before a website blocking order can be granted in a trademark infringement case. The English High Court ruled that the conditions had been met and ordered the UK’s main ISPs to block access to websites selling counterfeit goods.



Key statistics on counterfeit products

-  December 2014: 20,000 counterfeit dolls of characters based on the Disney movie "Frozen" with a value €600,000 were seized in Dublin port.
-  December 2014: 2000 pairs of fake Nike runners worth €300,000 worth and originating in China were seized in Cork.
-  Those involved in the counterfeit market are often linked to other forms of organised crime.
-  Food fraud is a growing concern within the EU, UK and Ireland.
-  There are significant risks of counterfeit goods entering into the legitimate supply chain.
-  September/October 2014: Interpol operations White Mercury II and Black Poseidon III seized 12 million fake goods worth €37m.
-  "Not only are counterfeit beauty products on the rise, they also contain some pretty dangerous ingredients, like arsenic, mercury and cyanide" reported the BBC.
-  It is now estimated that the global total value of counterfeit and pirated products will reach USD \$1.77tr by 2015.
-  There is evidence of domestic EU production of counterfeit goods. This is now considered a cost-effective option by counterfeiters, with lower risks of detection by customs and lower transport costs.
-  Gartner estimate that intellectual property losses due to 3D printer counterfeiting could total \$100bn by 2018.
-  The internet acts as a major facilitator for the sale and distribution of counterfeit goods.
-  Misuse of certification labels: the food industry has seen a growth in foods marked as 'healthy' and 'organic'.
-  The second phase of the Tangier Med port is due for development. Once complete, Tangier-Med will be the biggest port in Africa. Only 15 km from the EU, it could offer additional opportunities to criminal networks to export larger amounts of counterfeit goods to the EU.

“The high profits and low risk associated with modest penalties and lax enforcement of IP crime has made this a major new business opportunity for organized crime networks”



Confiscation of the Proceeds of IP Crime, UNICRI and BASCAP

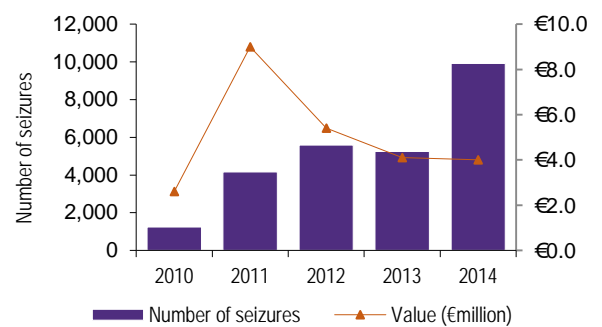
Enforcement

The Revenue Customs Service and An Garda Síochána are both tasked with ensuring the effective enforcement of the legal framework protecting rights holders' intellectual property in Ireland. Revenue Customs focus on the points of importation into the country and An Garda Síochána focuses on the investigation of the importation and sale of counterfeit goods.

The enforcement agencies continue their efforts to combat illicit trade, targeting counterfeit goods at the point of importation. The number of seizures of counterfeit goods has grown by nearly 700% from 1,245 in 2010 to 9,915 in 2014. Reflecting the growth of internet purchasing in this market, the bulk of the seizures made were of items arriving into the country by post⁵¹.

Steps are now being taken by major e-commerce sites to combat counterfeiting. It is reported that Alibaba took down 114 million websites in a period of only ten months.

Figure 7.3: Revenue seizures of counterfeit goods, 2010 to 2014



Source: Revenue Commissioners

Amazon are constantly working to improve monitoring software to remove counterfeit products and Ebay offer VERO Design Protocol, a subscription service allowing rights holders to check items being sold and notify eBay if they are counterfeit. If this is the case, Ebay will remove them from the listing.

Table 7.1: Seizures of counterfeit goods, 2010 to 2014

	2010	2011	2012	2013	2014
Number of seizures	1,245	4,166	5,580	5,246	9,915
Number of items	not available	not available	142,100	16,298	90,753
Value (€m)	€2.6m	€9.0m	€5.4m	€4.1m	€4.0m
Main categories of goods seized	Cosmetics, packaging/labels, jewelry, DVDs, footwear, toys, bags, phones and medicines	Cosmetics, clothing, and footwear and fashion accessories	Body care products, shoes and clothing, mobile phones and other electronic goods	Children's fashion clothing, toys and DVDs	Cosmetics, clothing, sports shoes, mobile phones and accessories and toys

Source: Revenue Commissioners

Cost to the economy

In 2008, the OECD estimated the total size of counterfeiting and piracy worldwide to be approximately US\$650 billion. The BASCAP updated this estimate for 2015 to a value of US\$1.77tr. This illustrates the alarming increase in this activity over a seven year period.

Table 7.2: Estimate of the total value of counterfeit and pirated products in 2008 and 2015

OECD Category	OECD est. \$bn (2008)	BASCAP est. \$bn (2015)
Internationally traded counterfeit and pirated products	\$285-\$360	\$770-\$960
Domestically produced and consumed counterfeit and pirated products	\$30 - \$75	\$80 - \$240
Sub total	\$455 - \$650	\$1,220 - \$1,770
Broader economy wide effects*	* \$125	\$125 +
Employment losses**	** 2.5 million	2.5 million +

* Effects on government tax revenues, welfare spending, costs of crime health services, FDI flows ** Estimate limited to G20 economies
Source: Frontier Economics

The Irish economy

It is difficult to determine the costs of illicit trade on industry and on the Exchequer, especially given that the market is largely unrecorded.

When we review counterfeit activities in isolation the statistics would indicate an estimated loss of revenue in the order of €300m to industry and an estimated loss of €70m in VAT receipts to the Exchequer .

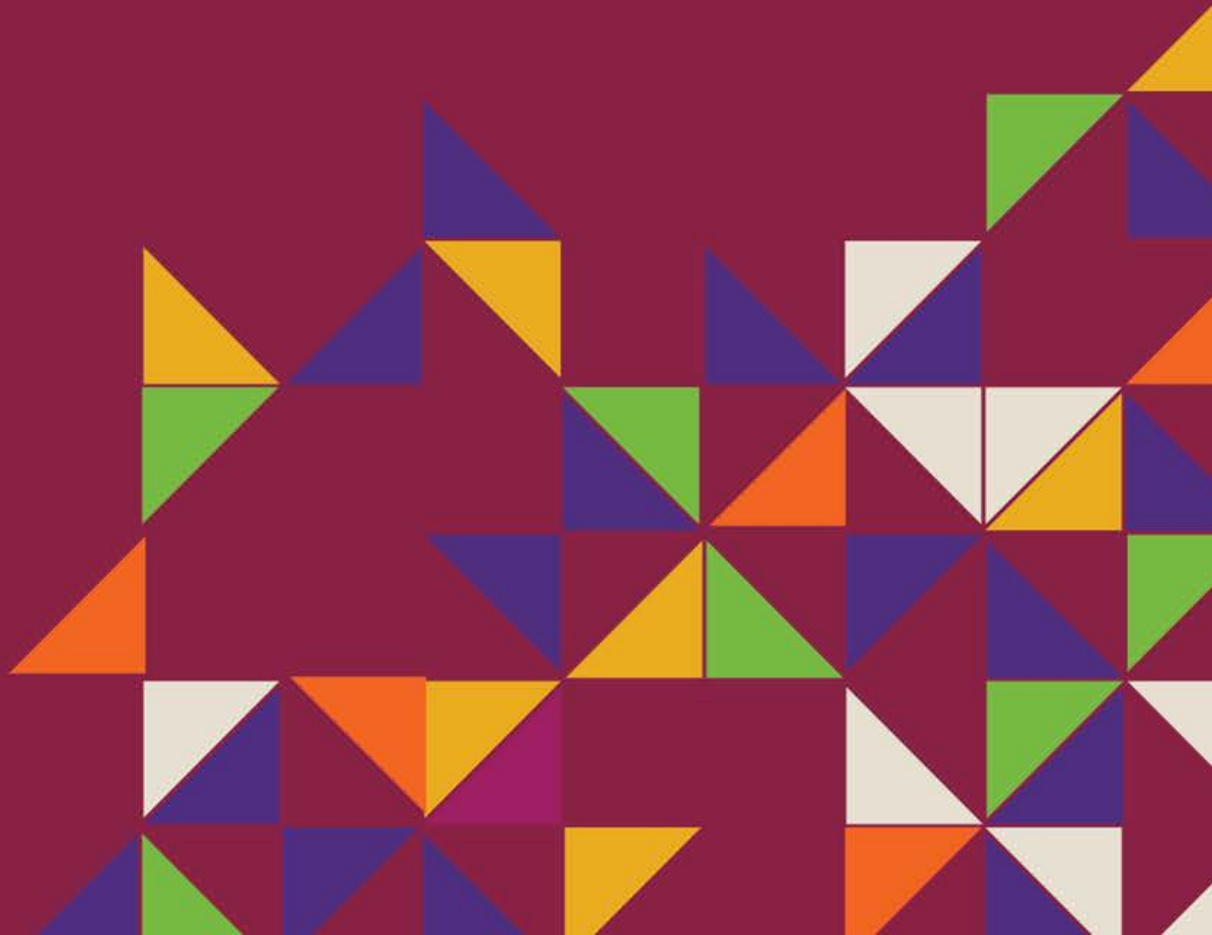
Apart from losses to manufacturers, retailers and the Exchequer, counterfeit goods can pose major health and safety risks which are not accounted for in the statistics.

Table 7.3: Estimate of the value of counterfeit only products

Counterfeit product	Value \$bn
Electronics	169.00
Foods	49.00
Autoparts	45.00
Toys	34.00
Clothing	12.00
Fake shoes	12.00
Sporting goods	6.50
Pesticides	5.80
Cosmetics	3.00
Aircraft parts	2.00
Watches	1.00
Money	0.81
Purses	0.70
Lighters	0.42
Batteries	0.23
Global counterfeit market total value (\$)	\$341.46
Ireland: counterfeit market total value	\$0.34
Ireland: counterfeit market total value (€)	€0.30
Ireland: estimated lost revenues VAT receipts	€0.07

Source: Havoscope, Global Black Market Information and Grant Thornton analysis

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