

The Illegal Cigarette Underground Economy in Indonesia: A Threat to National Economic Security from an Intelligence Perspective

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Abstract

The illegal cigarette underground economy erodes state revenues, distorts the market, and threatens national economic stability through the practice of cigarette production and distribution by avoiding excise/tax levies and regulations. This study aims to analyze the threat of these illegal economic practices from an intelligence perspective. This research focuses on identifying causal factors, modes of practice, and their impact on national economic security, as well as intelligence analysis to formulate countermeasures. The research method uses descriptive qualitative through interviews, observations, and literature studies. The findings revealed five causal source factors, seven modes of practice, and three harmful impacts. Hank Prunckun and Robert Ring's threat assessment model places the underground economy practice of illegal cigarettes as a serious/high level threat. Intelligence analysis detected a potential state loss due to illegal cigarettes of Rp18.46 trillion in 2023, the level of cigarette consumption of the population that has not fallen, and a depressed legal cigarette industry, which can threaten the stability of the state budget and national development. Strengthening inter-agency collaboration and synergy, enhancing the role of customs and excise intelligence, community mobilization, and appropriate excise tariff policies are needed in an effort to confront and tackle that illegal practice.

1. Introduction

Economic security is an integral part of national security, which is necessary in order to maintain the strength and sovereignty of the state (Buzan, 1991). Economic security refers to efforts to achieve and maintain the country's economic stability as part of a national security strategy, which affects the stability, strength and sovereignty of a country (Ronis, 2011). A country's economic security, which includes the availability of capital, a healthy and favorable business climate, the availability of jobs, and the sustainability of state revenues, will have an impact on the country's ability to maintain its military power. To achieve economic security, access to financial resources is needed through the State Revenue and Expenditure Budget (APBN). In Indonesia, 84.2% of state revenue in the state budget comes from tax revenues, which include various types of taxes, import duties, export duties, and excise duties (Ministry of Finance, 2024).

Tax revenues are generally obtained from economic activities, both in the form of production, distribution, and consumption activities. To regulate the course of these economic activities, the state establishes legal rules to maintain the continuity of national interests and security. Hidden economic activities that escape the supervision of state authorities or commonly referred to as the underground

economy, can be a threat to the realization of government policies and state revenue targets. According to Bajada in Marhamah and Zulaikha (2021), the underground economic activities emerged as a vehicle for economic actors to avoid government inspections and regulations. Smith in Faal (2003) defines the underground economy as the activity of producing goods and services on the basis of market prices, both legal and illegal but not recorded in the statistics of calculating Gross Domestic Product (GDP). Susanto in Amalia et al. (2020) stated that the underground economy is a part of economic activities that are deliberately hidden to avoid taxes and regulations, or because the goods and services produced are illegal. Piracy, smuggling, gambling, prostitution, as well as human trafficking, narcotics, and other illicit goods are examples of the underground economy (Nizar & Purnomo, 2011; Amalia et al., 2020). Another phenomenon of economic activities in Indonesia that can be categorized as an underground economy is the circulation of illegal cigarettes. Underground economy activities in Indonesia have a high value, which is not detected by the government, so that it distorts the performance of economic growth or GDP, one of which comes from illegal economic activities that have a negative impact on society such as illegal cigarettes (Kompas.id, 2024).

Illegal cigarettes are produced and distributed illegally, and circulate without fulfilling the obligation to pay state levies in the form of excise, VAT HT, and cigarette taxes, so the price can be cheaper than legal (official) cigarettes. In fact, state revenue from the cigarette excise sector is highly relied upon by the government to support the state budget, which has a value of 230.4 trillion rupiah or 10% of total tax revenue. According to Kasri et al. (2021), the number of illegal cigarettes in Indonesia is high and continues to increase, which contributes to a large loss of government revenue, ranging from 24.2 to 42 trillion rupiah, which is equivalent to 15.8% to 27.5% of cigarette excise revenue in 2018. The results of the Illegal Cigarette Survey conducted by Gadjah Mada University (UGM) show that the circulation rate of illegal cigarettes in Indonesia was 5.5% in 2022, then increased in 2023 to 6.89%. National cigarette production tends to decline by 323.9 billion cigarettes in 2022 which then in 2023 decreases to 318.2 billion cigarettes (DataIndonesia.id, 2024). However, the decline in production is not accompanied by a decrease in the percentage of smoking in the population, which according to data from the Central Statistics Agency tends to remain constant, namely 28.26% in 2022 and 28.62% in 2023. This indicates the population is still consuming illegal cigarettes.

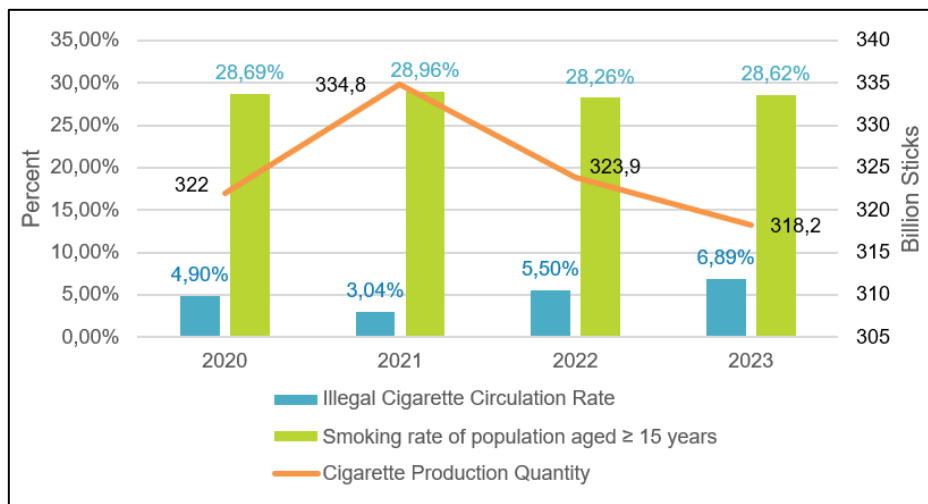


Figure 1. Cigarette Production, Cigarette Consumption, and Circulation of Illegal Cigarettes

The enforcement on illegal cigarettes is increasing year by year, but illegal cigarettes still exist and have even increased in recent years. This indicates that there is a considerable volume of illegal cigarette underground economy, which has not been fully recognized by the government. Another fact that needs attention is that in 2023 and 2024 the cigarette excise revenue target was not achieved 100%, only realized 98% in 2023 and 94.12% in 2024.

The failure to achieve the cigarette excise revenue target and the loss of state revenue due to the circulation of illegal cigarettes has great potential to be a threat to national economic security. Intelligence must be able to be present in securing state revenue from everything that has the potential to threaten the national interest (Siswosoemarto, 2012). This study aims to analyze the threats arising from the existence of the illegal cigarette underground economy to national economic security from an intelligence

perspective. With a qualitative approach, this study uses the threat assessment model of Prunckun and Robert Ring to determine the level of threat, then uses intelligence analysis in examining the phenomenon of the underground economy of illegal cigarettes in Indonesia to obtain knowledge that can be used to support efforts to prevent and overcome the threat of illegal practices.

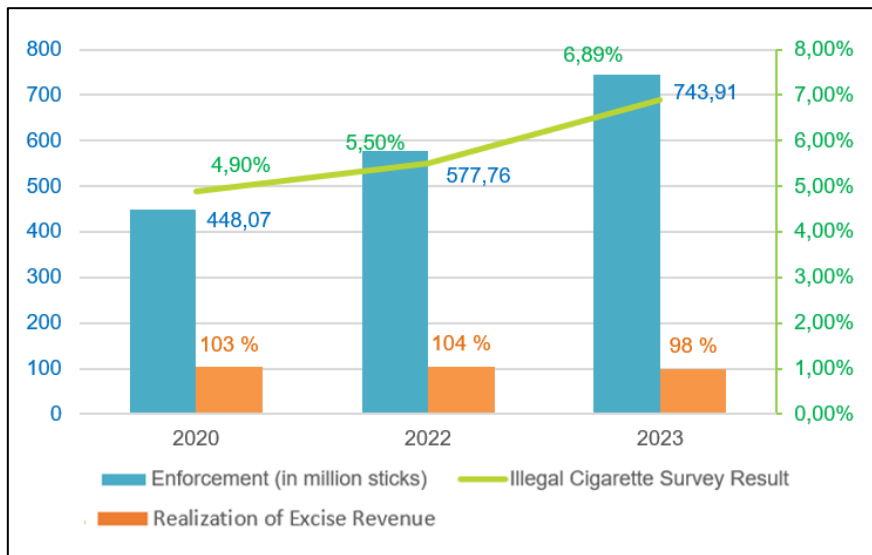


Figure 2. Levels of Circulation and Enforcement of Illegal Cigarettes, and Realization of Cigarette Excise Revenue

2. Literature Review

2.1. Threat

Soekarno (2014) explains the definition of threat as a thing, circumstance, incident, activity, or action that can harm, difficulty, annoy, cause pain, and harm. According to Soekarno (2011), there are three main criteria for threats, namely the source of the threat, the form of the threat, and the target of the threat. The source of the threat is oriented about the cause of the threat. The form of threat is oriented about how the threat is carried out. The threat target is oriented to the object or purpose for which the threat is carried out (the impact of the danger). Threats can be made by agents (perpetrators) of threats with their intentions and capabilities, against most entities, both to people, organizations, and the state (Prunckun, 2019). To weigh whether the threat actor has the intention and ability, Hank Prunckun establishes two important things for each of these factors: desire and expectation for intention, and knowledge and resources for ability. Soegirman (2009) stated that it is necessary to classify the level of threat danger so that in dealing with it it can be proportionate, not less, not overdose, effective, and not cause new problems, one of which can use the concept of Robert Ring's threat level which classifies threats into 4 (four) levels, namely minor, moderate, serious, and critical according to the level of danger to the target of the threat.

2.2. Intelligence

Intelligence is directly or indirectly related to national interest and national security (Sukarno, 2014). Intelligence plays a role in early detection and early warning to know, avoid, prevent, face, and overcome threats through intelligence functions, namely investigation, security, and mobilization (lidpamgal) to uphold national security and support the achievement of national welfare (Sukarno, 2014). Intelligence analysis is an analysis of something that is carried out based on an intelligence perspective that includes four analytical tools, namely early detection, early warning, problem solving, and forecasting (STIN, 2024).

2.3. Excise

According to the Organisation for Economic Co-operation and Development (OECD), excise is a fiscal instrument that has a role to regulate goods or services (Sunaryo et al., 2019). According to Law Number 39 of 2007 concerning amendments to Law Number 11 of 1995 concerning Excise, the definition of excise

is a state levy imposed on certain goods that have certain properties or characteristics, namely their consumption needs to be controlled, their circulation needs to be supervised, their use can have a negative impact on society or the environment; or its use needs to be imposed by the state levy for the sake of justice and balance. The purpose of excise duty is as a budget and a regular function (Lorosae, 2022). As a budget, it is to obtain state revenue, while as a regular, it is to regulate and control economic activities, both production, distribution, and consumption of goods (Beacukai.go.id, 2020). Excisable Goods (BKC) in Indonesia consist of ethyl alcohol, beverages containing ethyl alcohol, tobacco products that include various types of cigarettes such as cigarettes, cigars, leaf cigarettes, sliced tobacco, and other tobacco processing products, as well as the latest plastic and packaged sweetened beverages (MBDK). For BKC in the form of cigarettes, the excise payment is carried out by attaching an excise tape to the packaging of the retail sale of cigarettes in accordance with applicable provisions (Permenkeu 68/PMK.04/2018, 2018).

3. Method

This study uses a qualitative descriptive method. Qualitative methods are used to gain an in-depth understanding of the topic being researched. Data were collected by conducting interviews, observations, and literature studies. Interviews were conducted with informants consisting of policy makers, academics, and practitioners, as well as actors. Observations were made on the production, distribution, and marketing/sale of illegal cigarettes. Literature studies are carried out by referring to data relevant to the research topic, sourced from books, journals, and opensource data on the internet. The validity of the data was checked by triangulating data sources and triangulating informants. Qualitative data analysis techniques use the Miles, Huberman & Saldana model which consists of data condensation, data display, and conclusion drawing/verification activities (Sugiyono, 2024). Intelligence analysis is carried out by referring to the results of discussions and research findings to reveal a problem phenomenon from an intelligence perspective in the form of early detection, early warning, problem solving, and forecasting of the threat of the underground economy of illegal cigarettes.

4. Results and Discussion

4.1. The Threat of the Underground Economy of Illegal Cigarettes

The underground economy activities of illegal cigarettes cannot be separated from the demand and supply factors. Some Indonesian people consume illegal cigarettes because the price is more affordable, then the producers/importers provide the goods and distribute them to consumers. The flow of illegal economic activities consists of production and smuggling, distribution, marketing/sales, and consumption by the public. The perpetrators use various modes in carrying out production, import, and distribution activities so that the illegal cigarettes can eventually be circulated and consumed by the public.

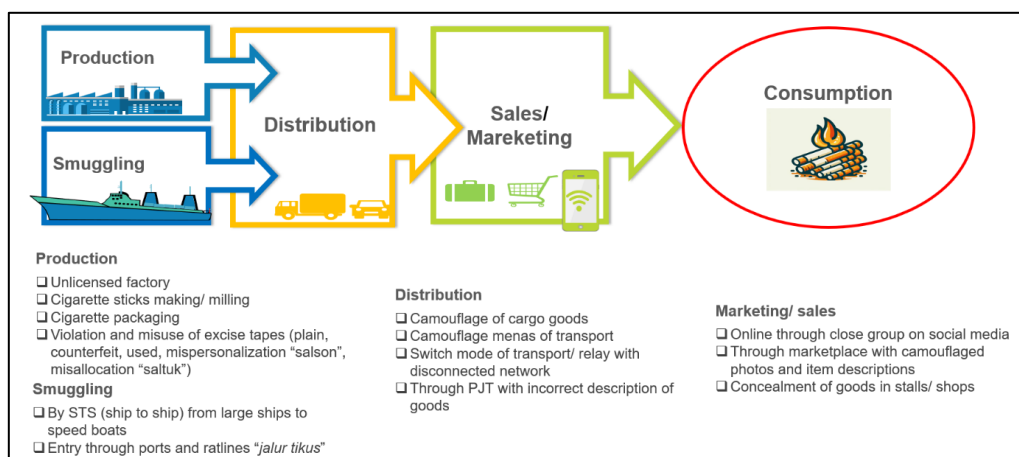


Figure 3. Underground Economy Flow of Illegal Cigarettes

In its circulation, illegal cigarettes have characteristics that can be recognized from the aspect of excise tape that is attached/should be attached to the retail packaging (packaging) of cigarettes. From the aspect of this excise tape, it can also be known the types of violations that show a product is circulating illegally. The types of violations of the excise tape attachment provisions include:

- 1) Plain: Cigarettes that are not attached to a tax tape.
- 2) Counterfeit: Cigarettes with fake excise tape attached.
- 3) Used: Cigarettes that are attached with used excise tape/ excise tape that is used repeatedly.
- 4) Mispersonalization (Salson)

Excise tape has a personalization code for each group II and III cigarette factory. Cigarette factories only have the right to attach excise tape to their products with excise tape that comply with the factory's personalization code. The excise tape must not be transferred between companies/factories. Wrong personalization (salson) is a cigarette product that is attached to an excise tape that is not his right (not his), for example a cigarette product using an excise tape from another company/factory whose excise rate is lower.

- 5) Misallocation (Saltuk)

Excise tape has a variety of model designs for each type of cigarette, where the design contains specific information about a cigarette product. The specific information includes the number of sticks per pack, the Retail Selling Price (HJE), and the type of cigarettes. The wrong designation (saltuk) is a cigarette that is attached to an excise tape that is not intended for it, for example Machine Kretek Cigarettes (SKM) products with high tariffs but attached to excise tape of Hand Kretek Cigarettes (SKT) which have low tariffs. Another example of a saltuk case is cigarettes with a content of 20 sticks per pack but attached to an excise tape that for cigarettes contains 12 sticks per pack, so the excise payment is lower.

The threat of the underground economy of illegal cigarettes can be described according to three main criteria consisting of the source of the threat (causative factor), the form of the threat (mode of practice), and the target of the threat (the impact of the danger). There are several factors that cause, mode of practice, and the harmful impact of the existence of the underground economy of illegal cigarettes as detailed in the table below.

Table 1. The Threat of the Underground Economy of Illegal Cigarettes

No	Threat Criteria	Research Results
1	Threat Source (Causal Factor)	<ul style="list-style-type: none"> • There is a demand for cheap cigarettes. • High excise rates and low purchasing power. • The socio-cultural conditions of the community that are permissive towards illegal cigarettes. • Profit motivation by way of excise/tax evasion. • Illegal importation and production of cigarettes.
2	Threat Mode (Mode of Practice)	<ul style="list-style-type: none"> • Cigarette smuggling. • Cigarette factories are not licensed. • Cigarette making: processing tobacco into cigarette sticks, otherwise known as "jahit" • Cigarette packaging: packaging cigarette sticks into retail packs or known as "nyontong" • Violation and abuse of excise tape. • Camouflage in distribution and marketing/sales. • With the backing (beking) of the local social environment and some state officials.
3	Threat Target (Hazard Impact)	<ul style="list-style-type: none"> • Threatening the stability of state revenues from excise and taxes. • Threatening the survival of the national cigarette industry and workforce. • Threatening the effectiveness of controlling cigarette consumption.

4.2. Threat Assessment of the Underground Economy of Illegal Cigarettes

4.2.1. Hank Prunckun's Model Threat Analysis

The underground economy activities of illegal cigarettes cannot be separated from the demand and supply factors. Some Indonesian people consume illegal cigarettes because the price is more affordable, then the producers/importers provide the goods and distribute them to consumers. The flow of illegal economic activities consists of production and smuggling, distribution, marketing/sales, and consumption by the public. The perpetrators use various modes in carrying out production, import, and distribution activities so that the illegal cigarettes can eventually be circulated and consumed by the public.

$$(Desire + Expectation) + (Knowledge + Resource) = Threat$$

Based on the results of the research, the perpetrator's desire is not to pay excise/taxes, and the hope is to make a profit. The perpetrator's knowledge is their skills and expertise in smuggling, producing, distributing, and marketing illegal cigarettes. Meanwhile, the resources of actors are human resources (workers and business networks), technology, machinery, means of transportation, raw materials, financial capital, and potential markets. The assessment of each threat factor to the practice of illegal cigarette underground economy is as follows:

- The desire is worth 5 (acute) because the perpetrator's desire not to pay or pay excise/excise duty is very high/acute, which underlies the perpetrators to carry out illegal cigarette underground economy activities. This indicates a significant intention to harm the targets, namely state revenue and tobacco consumption control.
- Expectations have a value of 3 (medium) because the expectations of actors to make profits are a common expectation for all business actors. This expectation also reflects an intention to achieve the desired goal, but the threat is medium in that it does not directly cause significant harm to the target.
- Knowledge is worth 4 (high) because the skills and expertise possessed by the perpetrator provide a high ability to run a business by avoiding taxes and regulation. This knowledge is considered a high threat because it shows a very significant ability to harm the target.
- Resources are valued at 4 (high) because workers, entrepreneur networks, technology, machinery, transportation facilities, raw materials, financial capital and potential markets owned by actors strongly support the practice of excise/tax evasion through the underground economy. These resources provide a high ability for the perpetrator to survive carrying out their actions, thus providing a high threat that endangers the target.

Table 2. Threat Assessment of the Illegal Cigarettes Underground Economy

Factor	Research Results	Value
Intention	Desire	Do not pay or pay minimum excise/tax. 5
	Expectation	Profit. 3
Ability	Knowledge	Skills and expertise in smuggling, producing, distributing, and marketing illegal cigarettes. 4
	Resources	Human resources (workers and business networks), technology, machinery, means of transportation, raw materials, financial capital, and potential markets. 4
Threat Coefficient Scale (Intent + Ability)		16
Threat Level		High

The assessment of the desire factors (5), expectations (3), knowledge (4), and resources (4) mentioned above resulted in a threat coefficient scale value of 16 (sixteen). Prunckun (2019) divides the threat level based on the value of the threat coefficient scale which consists of negligible level with a scale of 4-6, minimum level with a scale of 7-10, medium level with a scale of 11-15, high level with a scale of 16-18, and acute level with a scale of 19-20. The value of the threat coefficient scale of the illegal cigarette underground economy is 16, so it can be assessed as a high-level threat.

4.2.2. Robert Ring's Model Threat Assessment

Robert Ring divides threats into four levels based on the goals or impacts caused by the threat, from the lowest, which is minor, moderate, serious, to the highest is the critical level. A threat is classified as a serious threat to a critical level if the target concerns the existence, integrity and sovereignty of the Unitary State of the Republic of Indonesia (NKRI). Meanwhile, a threat can be classified as a moderate to serious level threat if it hinders the pace of national development programs, and state symbols include vital objects. Furthermore, at a lower level, namely a moderate threat, let alone a minor one, if the threat targets even lower devices such as regional infrastructure, programs in the region, and other regional devices. However, especially for corruption, it is classified as a serious threat because it can weaken and even knock down the joints of state life (Sugirman, 2009).

The results of the study show that the practice of illegal cigarette underground economy has a serious impact on national interests. This impact is considered to be able to hinder the pace of national development programs, so that the threat of the underground economy of illegal cigarettes is classified as a serious threat. From the results of the analysis carried out, the impact of the underground economy of illegal cigarettes can hinder the pace of national development programs due to the lack of state revenue from the excise and tobacco product tax sectors. National development programs, which are mostly funded by the State Budget, can be hampered if the stability of state revenues is not maintained. The underground economy of illegal cigarettes is also inseparable from the practice of backing (beking) which indicates the abuse of authority by state officials so that it can weaken or collapse the joints of state life. Therefore, based on the indicators determined by Robert Ring, the underground economy of illegal cigarettes can be categorized as a serious level of threat, which threatens national interests/security, especially in the economic field.

4.3. Intelligence Analysis

4.3.1. Early Detection

From the results of this study, it can be seen that the underground economy of illegal cigarettes is an illegal economic activity carried out to avoid excise/tax payments so as to harm the state finances and the national cigarette industry. These illegal activities also hinder cigarette consumption control policies that have negative effects on public health. Excise as a state levy that doubles as a tool of state revenue and a means of consumption control, is threatened to not function optimally due to the existence of an underground economy of illegal cigarettes. The impact of the underground economy of illegal cigarettes poses a threat to national interests and security, especially in the dimension of economic security. National economic security is supported by the availability of state budget funds to finance government programs and drive the national economy. Currently, state revenue from excise on tobacco/cigarette products is still one of the major contributors to the state budget, so its stability must be maintained.

The underground economy of illegal cigarettes also contributed to the failure to achieve cigarette excise revenue in 2023. Based on the 2023 UGM Illegal Cigarette Survey, the circulation rate of illegal cigarettes in Indonesia reached 6.87%, with the proportion of violations of 42.68% in the form of plain (polos) cigarettes, 34.87% saltuk cigarettes, 16.79% salson cigarettes, 4.22% cigarettes with fake/counterfeit excise tape, and 1.45% cigarettes with used excise tape. With the total national cigarette production in 2023 of 318.15 billion cigarettes, the illegal cigarettes in circulation are estimated to reach 23.46 billion cigarettes.

Table 3. Estimated Potential State Losses Due to Illegal Cigarettes in 2023

Types of Violations		Illegal Cigarettes (billion sticks)	Excise (billion)	VAT Cigarette (billion)	Cigarette Tax (billion)	Total State Levels (billion)
Plain (Polos)	42.68%	10.02	Rp 7.472,44	Rp 1.368,48	Rp 747,24	Rp 9.588,16
Misallocatino (Saltuk)	34.87%	8.18	Rp 4.280,09	Rp 417,25	Rp 428,01	Rp 5.125,34
Mispersonalization (Salson)	16.79%	3.94	Rp 2.060,87	Rp 200,91	Rp 206,09	Rp 2.467,87
Couterfeit (Palsu)	4.22%	0.99	Rp 738,84	Rp 135,31	Rp 73,88	Rp 948,03
Used (Bekas)	1.45%	0.34	Rp 253,87	Rp 46,49	Rp 25,39	Rp 325,75
	Total	23.47	Rp 14.806,11	Rp 2.168,43	Rp 1.480,61	Rp 18.455,15

By referring to the data on the proportion of types of violations as a result of the 2023 UGM Illegal Cigarette Survey, it is then calculated based on the lowest rate of the 2023 SKM in accordance with PMK No.109/PMK.010/2022, PMK No.191/PMK.010/2022, PMK No. 63/63/PMK.03/2022, and Law No.1 of 2022, where the VAT rate is 9.9% of the HJE and the cigarette tax rate is 10% of the excise value, then the potential value of state revenue lost due to the circulation of illegal cigarettes during 2023 is Rp. 18.46 trillion, consisting of excise of Rp. 14.8 trillion, VAT HT of Rp. 2.17 trillion, and cigarette tax of Rp. 1.48 trillion. The calculation of the value of the country's potential losses has not taken into account the value of losses caused by the loss of the legal cigarette market caused by the circulation of illegal cigarettes, the closure of official factories due to the inability to compete with illegal cigarettes, and the negative effects in terms of health that are not monitored due to the circulation of illegal cigarettes. The results of the threat analysis of the Hank Prunckun and Robert Ring model stated that the threat of the underground economy of illegal cigarettes is considered a high-level/serious threat.

4.3.2. Early Warning

In the discussion of this study, there are three harmful impacts that are targeted by the underground economy of illegal cigarettes, namely threatening the stability of state revenues from excise/taxes, threatening the continuity of the national cigarette industry and labor, and threatening the effectiveness of tobacco consumption control policies. The disturbed revenue stability will have an impact on the decline in the performance of the State Budget in financing national development programs. The declining productivity of the national cigarette industry will cause labor absorption to decrease, which can result in an increase in the unemployment rate. Uncontrolled and continuously increasing cigarette consumption will make the level of public health decrease. The results of the threat analysis of the Robert Ring model show that the threat posed by the underground economy practice of illegal cigarettes has a serious impact on national interests because it is considered to be able to hinder the pace of national development programs.

Data from the UGM illegal cigarette survey in the last three years as well as data on the results of cracking down on illegal cigarettes show that there is an increasing volume of illegal cigarette underground economy. Contrary to this, national cigarette production data, cigarette excise revenue data, tobacco processing industry labor data, and tobacco processing industry contribution data to GDP, which shows a decline in the last year (Figure 5). In fact, BPS data shows that the percentage of the population smoking as well as the average consumption and per capita expenditure per week for cigarettes tend to increase in the last year (Figure 4). This indicates an increase in the circulation of illegal cigarettes which fills the market share of legal cigarettes which has decreased. The underground economy of illegal cigarettes that continues to grow will have a fatal impact on national economic interests/security, such as declining cigarette excise revenues, declining absorption of cigarette industry workers, and uncontrolled public cigarette consumption.

Cigarette excise revenues that fall and do not reach the set target will have an impact on the increasing lack of funds (deficit) in the State Budget. This can result in delays in government programs, or budget cuts so that the planned development programs cannot be realized optimally. The shortage of state budget funds will also encourage the government to increase debt. The debt will create the burden of installment and interest payments in the next few years, thereby narrowing fiscal space and reducing the country's preparedness to face future uncertain situations. The continuous decline in the productivity of cigarette factories will lead to the closure of cigarette factories because the business is no longer profitable. The

closure of cigarette factories will result in the loss of jobs that have absorbed a lot of labor. There can be layoffs that increase the unemployment rate and have the potential to cause social turmoil. The closed cigarette industry will also contribute to reducing national GDP. The uncontrolled and increasing consumption of cigarettes will cause the negative impact on health to also increase. The risk of people getting diseases due to cigarette consumption will be higher, which can cause people's productivity to decrease. Declining public productivity can hinder national economic growth. These impacts will be more severe if the developing underground economy of illegal cigarettes is cigarette smuggling, which has no contribution at all to the absorption of production labor and the absorption of tobacco raw materials from domestic agriculture.

4.3.3. Problem Solving

To overcome the threat of the underground economy of illegal cigarettes, a strategy is needed by considering the causative factors and how these illegal practices are carried out. From the results of the research discussion, the threat of the underground economy of illegal cigarettes comes from the import and production of illegal cigarettes, which is driven by the demand for cheap cigarettes, the existence of high excise rates and low purchasing power, profit motivation by way of excise/tax evasion, and the socio-cultural conditions of the community that are permissive towards illegal cigarettes. The mode of illegal practice is carried out by smuggling cigarettes, unlicensed cigarette factories, cigarette making (jahit), cigarette packaging (nyontong), violation and abuse of excise tape, camouflage of distribution and marketing/sales, as well as support (beking) from the surrounding social environment and some state officials. Therefore, strategies to overcome the problem of illegal cigarettes must be oriented to minimize the causative factors and opportunities for perpetrators to carry out their practices.

The causative factor that can be directly intervened by the government is the excise rate, so the strategy of determining the right and balanced excise rate must be carried out in accordance with the national interest. The high excise tariff policy is inseparable from international pressure to campaign against tobacco through the WHO in the Framework Convention on Tobacco Control (FCTC). Indonesia must be able to reduce this pressure while still prioritizing Indonesia's national interests as a producer of tobacco and clove cigarettes. The amount of excise tariffs must consider the purchasing power of the public and the ability of state officials to oversee its implementation so that it does not develop towards an underground economy. To overcome the perpetrators who carry out illegal practices, strict law enforcement must be carried out. To change the perception of the public who tend to be permissive towards illegal cigarettes, it is necessary to mobilize by utilizing excise funds for programs whose benefits can be directly felt by the community so that moral awareness and concern for the legality of cigarettes arise. To implement the general solution orientation above, based on the results of the research, the following recommendations can be given:

1) Strengthening Inter-Agency Collaboration and Synergy

Collaboration and synergy between the Directorate General of Customs and Excise (DJBC) and other law enforcement agencies such as the POLRI, TNI, Satpol PP, as well as related agencies such as PPATK and BIN, are key to strengthening supervision and law enforcement against illegal cigarettes. This collaboration and synergy between institutions is to increase the scope of supervision, especially in border areas that are prone to smuggling and in inland areas that are prone to the circulation of illegal cigarettes. This form of cooperation allows for cross-sector coordination to share information, resources, and strategies in dealing with illegal cigarette underground economy actors. Collaboration and synergy can encourage all agencies to have the same commitment to the eradication of illegal cigarettes. Synergy in the form of joint operations also needs to be increased to overcome the presence of officials involved in illegal activities, as well as to face resistance from the community.

2) Enhancing the Role of Customs and Excise Intelligence

DJBC as the main element of carrying out duties and functions in the field of customs and excise, has great challenges in dealing with the threat of the underground economy of illegal cigarettes sourced from within the country and abroad. Indonesia's very wide geographical conditions with long land and sea borders, and supported by a large population as a very potential market, make Indonesia vulnerable to the practice of illegal cigarette underground economy. DJBC as the holder of *lex specialis* authority over excise, is the main initiator in eradicating illegal cigarettes. In order for enforcement operations in the context of law enforcement to run effectively and efficiently, accurate and appropriate intelligence information is needed. Customs and excise intelligence needs to adapt to the

development of current modus operandi and technology. The underground economy of illegal cigarettes as a form of economic crime will be closely related to financial transactions, which based on the results of this study, are mostly carried out electronically (transfers). Communication channels between actors are also mostly carried out electronically (online), without having to meet to make transactions. Therefore, enhancing the role of customs and excise intelligence in terms of transaction analysis and electronic communication is very necessary. Customs and excise intelligence operations also need to cover all aspects, namely follow the goods, transportation, documents, people, and money. By mastering these 5 aspects, supervision and law enforcement of the underground economy of illegal cigarettes can be maximized. Enhancing the role of intelligence is also carried out to guard the increase in excise rates which has the potential to encourage the emergence of the underground economy. Enhancing the role of intelligence can be carried out, one of which is through the development of an intelligence organization at DJBC with the establishment of a directorate (echelon level II) that is specifically in charge of customs and excise intelligence. With the development of this organization, the role of customs and excise intelligence will be able to be improved and expanded, not only in information management, but also includes strategic policies, early detection and early prevention, agent coaching/development, the use of the latest technology, and cooperation between intelligence communities at a higher level. Customs and excise intelligence is required to be able to analyze transactions and communications related to the underground economy of illegal cigarettes. Customs and excise intelligence also needs to place agents at ports/warehouses located in countries around Indonesia's borders such as Singapore and Malaysia to detect the presence of illegal cigarettes to be sent to Indonesia.

3) Community Mobilization

Community mobilization is very important, because it is from the community that the demand for illegal cigarettes arises. The need for cheap cigarettes and economic motives make people less concerned about the legality of goods. People in the production area also have a perception that supports illegal cigarettes due to the economic and socio-cultural factors of the local environment. Therefore, in addition to strict law enforcement efforts, community mobilization efforts must be carried out. Mobilization can be done by utilizing excise funds for programs whose benefits can be felt directly by the community, such as access to health services, fuel/electricity subsidies, infrastructure development/public facilities, and educational assistance. These programs are socialized by bringing the narrative that the financing comes from cigarette excise. By feeling the direct benefits of cigarette excise funds, it is hoped that there will be moral awareness among the public who are able to change their perception to be anti-illegal cigarettes.

4) Proper excise rate policy

In dealing with the circulation of illegal cigarettes, the right excise rate policy is very necessary. Currently, the cigarette excise tariff policy uses a Laffer Curve approach by considering 4 aspects, namely state revenue, consumption control, labor continuity, and supervision of illegal cigarettes. Too high a tariff can trigger the emergence of illegal cigarettes due to the significant price difference between legal and illegal cigarettes. Excise tariff policies must also consider people's purchasing power. The increase in excise rates that are not balanced with people's purchasing power will cause a shift in consumption to cigarettes that are cheaper, even to illegal cigarettes. The excise rates set should not burden legal cigarette producers too much, thus reducing the incentive to switch to illegal production. Seeing the trend of declining productivity of the national cigarette industry, declining excise revenue, and increasing circulation of illegal cigarettes, there should be no increase in cigarette excise rates for the time being, considering that people's purchasing power is still low.

4.3.4. Forecasting

The underground economy of illegal cigarettes in Indonesia experiences fluctuating developments every year. So on, the circulation of illegal cigarettes will still exist and will continue to experience fluctuating developments, depending on how the factors that affect it develop. Illegal cigarettes have the potential to increase when there is a new government policy that curbs cigarette products. As is the case with Government Regulation (PP) Number 28 of 2024 concerning Health which was lowered into the Draft Regulation of the Minister of Health (RPMenkes) which will further suppress legal cigarette products in terms of regulations. The underground economy of illegal cigarettes will grow as the pressure of regulatory burdens and excise/taxes increases. Law enforcement and supervision must continue to be strengthened to suppress the trend of illegal cigarette volumes in the future.

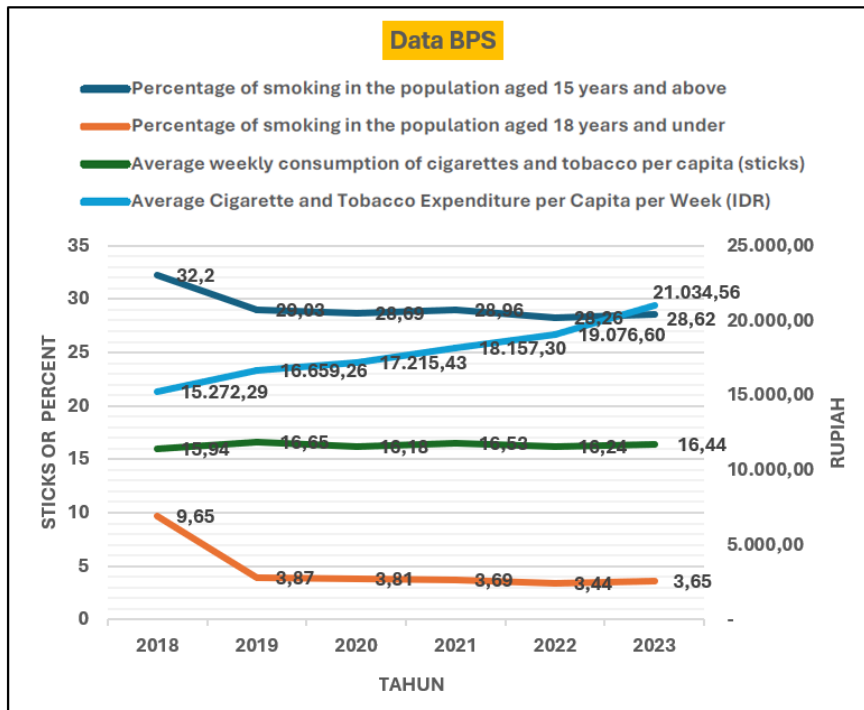


Figure 4. Cigarette Consumption Trends

Looking at the BPS data above, since 2019 the percentage of the population who smoke and the average per capita consumption per week of cigarettes is relatively fixed, which indicates that the level of people's cigarette consumption tends to be fixed. Seeing this, it can be assumed that the market (demand) for cigarettes is fixed, so that legal and illegal cigarettes will share the same market. If the productivity of legal cigarettes decreases, the market will be filled by illegal cigarettes, and vice versa if the productivity of legal cigarettes increases, then the market share of illegal cigarettes will decrease. Judging from these assumptions, it is important to always maintain the productivity of the legal cigarette industry.

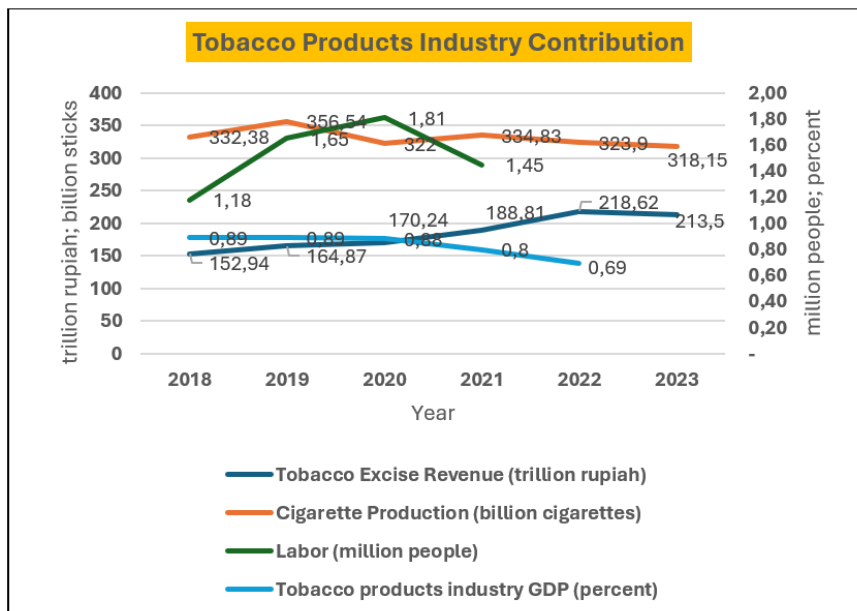


Figure 5. Trends in Tobacco Products Industry Contribution

The trend of the contribution of the tobacco product industry has decreased in the last year. The increase in high excise rates will suppress the productivity of legal cigarettes, which will result in an increase in illegal cigarettes. If left unchecked, state revenue will decrease, and the absorption of labor and tobacco from farmers will also decrease. This will be exacerbated if the illegal cigarettes that fill the market

are smuggled cigarettes from abroad, the impact will be more serious. When viewed from the level of losses to the national interest, smuggled cigarettes are the most detrimental threat both in terms of import duties, excise, taxes, absorption of production labor, and absorption of tobacco from farmers. The trend of cracking down on cigarette imports has increased, which means that the threat of imported cigarettes is increasingly obvious. The increasingly high price of legal cigarettes will encourage the entry of illegally imported cigarettes to compete in the domestic market. This needs to be a priority for early prevention.

The trend of increasing the volume of illegal cigarettes will make the cigarette excise revenue target not achieved and even more decreasing than in previous years, so that the state budget deficit is getting larger which has the potential to disrupt economic stability. Economic instability can occur when the state does not have enough funds to finance public programs and government operations due to insufficient state revenue. As a result, the government has to look for other sources of funding, for example by indebting to other countries or international financial institutions. Unfortunately, the position as a borrower of funds can make Indonesia forced to obey the wishes of the lender. They could have used this situation to dictate government policies in their own interests.

In order to maintain economic stability, efforts to maintain the productivity of the national cigarette industry must be carried out without increasing public cigarette consumption. The national cigarette industry is an industry that has existed since the 19th century and is integrated from upstream to downstream, which has contributed greatly to the national economy. Legal cigarettes must be given a realistic price, but also not cheap, so that later the market mechanism will automatically shift illegal cigarettes from the market. This effort must be balanced with increased supervision and law enforcement for illegal cigarette underground economy actors. Optimizing state revenue from other tobacco processing products such as various types of e-cigarettes must also be a concern of the government, considering that types of e-cigarettes are starting to be in demand by the public.

The dilemma of always balancing the revenue (budgetair) and control functions (regulerend) can lead to stagnation of excise/tax revenues in the future. In order to anticipate this and to increase state revenue, the government needs to be encouraged to immediately extend excise objects and other state revenue objects in order to ensure the availability of state budget funds. Sectors other than taxation need to be a serious concern for the government in exploring the potential for state revenue. The natural resources (SDA) sector can be an alternative for the government to maximize its management and contribution to state revenue for the prosperity of the Indonesian people.

5. Conclusion

The underground economy of illegal cigarettes constitutes a covert economic practice aimed at evading state levies and regulations, encompassing the smuggling, production, distribution, and marketing or sale of illicit cigarettes. The threat posed by this illegal practice is classified as a serious or high-level threat. The emergence of the illegal cigarette underground economy is driven by multiple factors, including demand for cheap cigarettes, high excise rates coupled with low purchasing power, a permissive sociocultural attitude toward illegal cigarettes, profit-driven motives through excise evasion, as well as the importation and production of illegal cigarettes. This threat manifests through various modes of practice, such as cigarette smuggling, unlicensed cigarette factories, illicit cigarette sticks production (jahit), illicit cigarette packaging (nyontong), violations and misuse of excise tape, camouflage of distribution and marketing/sales, as well as protection (beking) from local communities and some state officials. These activities endanger national economic security, specifically undermining the stability of state revenue from excise and taxes, threatening the sustainability of the national cigarette industry and its workforce, and reducing the effectiveness of cigarette consumption control. To address this threat, the government must focus on preventing cross-border smuggling and curbing domestic illicit production. Therefore, it is necessary to strengthen collaboration and synergy among agencies, enhance the role of customs and excise intelligence, mobilize public support, and implement appropriate excise tariff policies, to ensure more effective efforts in combating the underground economy of illegal cigarettes.

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