



18th November 2016

AACS SUBMISSION

Committee Secretary
Parliamentary Joint Committee on Law Enforcement
PO Box 6100
Parliament House
Canberra ACT 2600
le.committee@aph.gov.au

Re: Inquiry into illicit tobacco

On behalf of members of the Australasian Association of Convenience Stores (AACCS), we make the following subsequent submission to the Parliamentary Joint Committee on Law Enforcement regarding the inquiry into illicit tobacco in Australia.

The AACCS made an initial submission to the Committee earlier this year. The reasons for this subsequent submission are:

- The AACCS recently commissioned research into people's attitudes towards and awareness of illicit tobacco in Australia, the outcomes of which are relevant to this Inquiry; and
- We understand the next public hearing for the Inquiry is to be held on November 23, 2016 and on behalf of the AACCS, I offer to appear before the Committee to present this research, provide an update on the issue from the perspective of our members, and answer any questions the Committee has.

As the peak body for the convenience industry in Australia, we are in the unique position of being able to provide actual real world evidence of the impact of the growth in the illicit tobacco market on retailers.

In this submission, we address several of the Terms of Reference guiding the inquiry, offer a unique retailer insight into the impact of policies like plain packaging on illicit tobacco, while offering some potential solutions to tackle the illicit tobacco market.

It is impossible to discuss the subject of illicit tobacco in Australia without referencing the impact that plain packaging legislation has had on the black market for tobacco.

Since the introduction of plain packaging, Australia has become one of the most profitable markets for criminals involved in the importation and sale of illegal tobacco products.

Regular, major seizures of contraband tobacco at our borders highlight the enormity of the illicit tobacco market in Australia. While police and customs officials should be commended for these operations, the sheer size and scope of illegal tobacco operations is impossible to control entirely.

Regrettably, existing Government policy including relentless legal tobacco excise increases is putting further pressure on the legal tobacco market and heightening the demand for illicit tobacco among otherwise law-abiding consumers.

The evidence on this score is clear: the more tax is applied to a packet of cigarettes, the more consumers will seek cheaper and potentially illegal alternatives. Criminal gangs have shown they are not only willing but very capable of filling any gaps in the legal tobacco market.

But the impacts on crime do not end there. The excise increases on tobacco coincide directly with rises in robberies targeting tobacco products specifically. This threatens the safety of convenience retailers and puts them at very serious risk of violent crime.

Illicit tobacco is by very definition non-compliant. There are no product quality controls and criminals have no issue in selling tobacco to minors. The proliferation of non-compliant tobacco products of dubious quality is the direct result of Government regulations surrounding the retail of legal tobacco in Australia.

At this point it's important to assert that the AACS is not an arm of, nor does it lobby on behalf of, the tobacco industry. It is the peak body for the convenience industry in Australia, representing the interests of some 6,000 stores.

The AACS wishes to thank the Committee for its consideration of our submission.

Yours sincerely,

Jeff Rogut FAIM MAICD
Chief Executive Officer
Australasian Association of Convenience Stores Limited

Website: www.aacs.org.au

About the AACS

The Australasian Association of Convenience Stores (AACS) is the peak body for the convenience industry in Australia.

Nationally, our industry employs over 40,000 people in over 6,000 stores. The majority of these stores operate as family run businesses, often under licence or franchise agreement, or independent ownership. They regularly employ family members and people from the local communities in which they operate.

The AACS represents the interests of these small businesses; their owners, staff, suppliers and customers.

The convenience industry in Australia was valued at approximately \$18 billion in 2015 according to companies contributing to the *2015 AACS Annual State of the Industry Report*. This report contains the most comprehensive information available on the convenience industry in Australia and we would be happy to provide a copy.

As an Association we enjoy strong ties with our international counterparts including the convenience stores associations in the US, Canada, the UK and New Zealand. We also visit similar stores in South East Asia to keep abreast of changing or emerging trends.

Executive summary

- Legal tobacco products represent a significant proportion of total convenience store sales in Australia. According to the most recent AACS State of the Industry¹ report, on average over 37% of a typical convenience store's sales and 25% of a store's gross profit comes from legal tobacco.
- Since the introduction of plain packaging for tobacco products in Australia in December 2012, the dollar volume of legal tobacco sold in our channel has remained stable. This is because of the tax increases placed on legal tobacco.
- However convenience stores have suffered as a result of an increase in the illicit trade of tobacco, with the volume of tobacco sold reduced. Increased product handling errors and increased labour and inventory management costs are other side effects of plain packaging.
- Awareness among small retailers in Australia of illicit tobacco is high and has increased since the introduction of plain packaging. Customers are aware of illicit tobacco and some are actively seeking it out.
- As at October 2015, the illicit tobacco market was estimated by KPMG² to account for 14.3% of total tobacco consumption nationally in the 12 months to June 2015.
- Sold legally, this would have generated an extra \$1.42 billion in tax revenue for the Australian Government.

¹ *The AACS State of the Industry Report 2015*

² *Illicit Tobacco in Australia 2015 Half Year Report*, KPMG

- Recent high profile seizures of illegal tobacco has reinforced the enormity of the illicit tobacco market in Australia.

Response to the Terms of Reference

In this submission, the AACS offers comments and its perspective on several Terms of Reference shaping the inquiry, namely:

- the loss of revenue to the Commonwealth arising from the consumption of illicit tobacco products;
- the involvement of organised crime, including international organised crime, in the importation, distribution and use of illicit tobacco in Australia; and
- the effectiveness of relevant Commonwealth legislation.

The loss of revenue to the Commonwealth arising from the consumption of illicit tobacco products

It's well known that excise from legal tobacco sales is a significant contributor to Government revenue.

What isn't as widely known is that the revenue the Government is missing out on because of the huge spike in illicit tobacco trade has run into the billions of dollars annually.

As at October 2015, the illicit tobacco market was estimated by KPMG² to account for 14.3% of total tobacco consumption nationally in the 12 months to June 2015.

Sold legally, this would have generated an extra \$1.42 billion in tax revenue for the Australian Government.

The involvement of organised crime, including international organised crime, in the importation, distribution and use of illicit tobacco in Australia

Criminal gangs are proven to be very effective in filling gaps in the legal tobacco market.

According to research from leading international research company Roy Morgan entitled *The Impact of Plain Packaging on Australian Small Retailers*³, commissioned by Philip Morris and supported by the AACS and other retail associations, a third of retailers reported having had customers enquire about purchasing illicit tobacco from their outlets.

The public is aware of the existence of illicit tobacco in Australia and are actively seeking it out, driven in part by the high cost of legal tobacco. However many consumers are unaware of the extent and prevalence of illicit tobacco in Australia⁴.

The Roy Morgan research also shows that awareness among small retailers in Australia of illicit tobacco is high and has increased since the introduction of plain packaging. More than four in ten retailers perceive illicit trade to be having a negative impact on their business.

³ *The Impact of Plain Packaging on Australian Small Retailers*, Roy Morgan, 2013

⁴ *E-cigarettes, illicit tobacco, sugar taxation and alcohol retailing – a public opinion survey*, Sexton Marketing Group for AACS, September 2016

The growth of the illicit market, combined with excessive taxation increases and plain packaging legislation, has resulted in a shift in consumer purchasing habits when it comes to tobacco.

Consumers are now driven predominantly by price as brands have been diminished, and adult consumers are increasingly looking at illicit products as tax hikes on legal tobacco continue to have a dramatic impact on price.

Of course, illicit products are much more likely to end up in the possession of minors, as these products by definition are not sold responsibly.

The effectiveness of relevant Commonwealth legislation

Recent high profile seizures of illegal tobacco have reinforced the enormity of the illicit tobacco market in Australia.

The unprecedented spike in the illicit tobacco market coincides directly with the introduction of plain packaging legislation and the regular excise increases applied to legal tobacco products.

It's important to understand that tobacco itself is, despite being more expensive in Australia than almost anywhere else in the world, actually a low margin product for retailers. The tax consumers pay on tobacco is what contributes to its high price and these high prices make Australia a particularly attractive market for criminals to sell illicit tobacco.

Illegal tobacco is by its very nature non-compliant with restricted sale and packaging requirements, and criminals have no issue selling illicit tobacco products to minors.

Existing regulations surrounding the sale of legal tobacco are not working. They are pushing otherwise law abiding consumers to the illicit market, and they are positioning Australia as one of the world's most lucrative markets for illegal tobacco.

The Australian Government is losing out. It's no secret excise from legal tobacco sales is a significant contributor to Government revenue. As at October 2015, the illicit tobacco market was estimated by KPMG² to account for 14.3% of total tobacco consumption nationally in the 12 months to June 2015.

Sold legally, this would have generated an extra \$1.42 billion in tax revenue for the Australian Government.

Legal tobacco is an extremely important product for convenience stores. Though it is low margin, it still represents a considerable proportion of sales and is a key reason for consumers to visit our members' stores.

The rise in the illicit tobacco market is hurting small businesses especially, as the major supermarket chains are much better positioned to absorb the regulatory costs and the loss of trade to the black market through their many other product categories and buying power.

New AACS research on illicit tobacco

In September 2016, new research commissioned by the AACS was released which gauged public opinion on the illicit tobacco trade and whether people felt more should be done to restrict it. It involved an opinion survey with a total of 4,000 Australian consumers aged 18+ years (and eligible to vote in State/Territory and Federal elections) participating.

A summary of the main findings of the research is below. I would be pleased to present the full detailed findings to the Committee at its earlier convenience.

- While consumers and retailers are very aware of illicit tobacco, consumer awareness of the extent of the illicit tobacco trade is low.
- The biggest single consumer concern is that illicit tobacco is a revenue-earner for organised crime, who use that revenue to expand their criminal activities, including into socially damaging areas like ice production and distribution.
- Most consumers would be concerned if politicians turned a blind eye to this issue, or worse still, did not adequately resource Customs to stop the trade at its source.
- There is strong support for tougher penalties for illegal tobacco trafficking and unscrupulous retailers selling illegal tobacco products.
- There is also concern that government revenue is being lost, putting pressure on budgets for hospitals, schools, etc.

Here is a selection of some of the more surprising – and concerning - findings of the research.

Incidence of being offered illegal cigarettes or illegal tobacco products to buy or try

	Smokers	Non-smokers	Total sample
Have been offered illegal tobacco products	22%	4%	7%
Have not been offered illegal tobacco products	72%	91%	88%
Unsure	6%	5%	5%
Total	100%	100%	100%

These results suggest that the illicit tobacco trade is not just about imports – with 22% of smokers and 4% of non-smokers having been offered illicit tobacco products to buy or try. They also suggest that illicit tobacco is being actively promoted, especially (but not exclusively) to smokers.

After being exposed to the issues associated with the illicit tobacco trade, what action, if any, do consumers believe the Government should be taking?

	Smokers	Non-smokers	Total sample
Should be taking urgent action	44%	51%	50%
Should be on a watch list	37%	38%	38%
Not requiring any significant action	10%	4%	5%
Undecided	9%	7%	7%
Total	100%	100%	100%

These results show that 50% of consumers think the Federal Government should be taking urgent action, with a further 38% believing it needs to be on a watch list, i.e. 88% of consumers want action of some sort to deal with this issue.

Do consumers feel strongly enough about the illicit tobacco trade for it to affect their vote at the next Federal election?

[Base = all voters]	Coalition voters	Labor voters	Greens voters	Other Party voters	Independent voters	Hard undecided voters	All voters
Yes	10%	10%	10%	5%	14%	5%	10%
Possibly	34%	37%	33%	37%	37%	25%	34%
No	46%	44%	46%	50%	41%	32%	44%
Unsure	10%	9%	11%	8%	8%	38%	12%
Total potential to influence votes	54%	56%	54%	50%	59%	68%	56%

Recommendations to tackle the illicit tobacco issue

The illicit tobacco market robs legitimate businesses of sales and market share and the Government of its entitled revenue from the sale of tobacco.

In an effort to crack down on the illicit trade of tobacco, a hotline for retailers and consumers to alert authorities to the illicit trade of tobacco could be established.

This would provide a low cost avenue for any retailer or consumer approached by an individual or group to purchase illicit tobacco products to assist police and Government in targeting the criminals involved in the illicit market.

The impact of plain packaging on the illicit tobacco market

Several years on from the introduction of tobacco plain packaging in Australia and the evidence to date validates what retailers were afraid of: that their businesses would suffer as a result of illicit trade, product handling errors and increased labour and inventory management costs.

The volume of legal tobacco sold by convenience stores in Australia is slightly down, however the dollar value of sales has increased, as excessive tax hikes continue to have a significant impact [see appendix – source: AACS State of the Industry Half year Snapshot 2016].

Since the introduction of plain packaging there has been a shift by customers to purchase cheaper brands, however the excessive taxes on tobacco products in Australia has impacted this too.

High tobacco prices have driven consumers to shop mainly on price, as brands have been substantially devalued by plain packaging. The extension of this consumer purchasing behavioural shift is that consumers are increasingly looking at cheaper alternatives including illicit products. Illicit products have a greater potential for being sold to minors, which is a major concern. In addition, the extent of robberies on convenience stores has risen substantially as criminal gangs focus on the lucrative tobacco products.

Honest retailers suffer as a result of all these factors.

The negative impacts of plain packaging for small retailers were always obvious to those in the industry. The rise in the illicit tobacco market is just one consequence of a policy implemented without consultation and consideration of the small business perspective.

Conclusion

The AACS, in its role as the representative and voice for convenience stores across the country, wishes to emphasise to the Committee the significant negative impact that the sharp rise in illicit tobacco trade in Australia continues to have on small retailers.

More than four in ten retailers perceive illicit trade to be having a negative impact on their business, and a third report having had customers enquire about purchasing illicit tobacco.

However, many consumers remain unaware of just how prevalent illicit tobacco is in Australia. The latest AACS research suggests that the issue has the potential to influence how people vote, and the potential votes influenced by this issue will only grow as awareness of the illicit trade of tobacco increases.

Recent large scale busts in Australia highlight the demand for, and prevalence of, illegal tobacco.

The huge growth in illicit tobacco sales is concerning for all. Police in Australia have made major seizures of illicit tobacco and worryingly it is quite easy, as some newspapers reporters have found, to buy non-compliant tobacco.

This impacts honest retailers who sell tobacco responsibly and legally as well as the Government, which experiences a significant loss of revenue because the sale of illicit tobacco circumvents the tax otherwise payable on legal tobacco products.

Yours sincerely,

Jeff Rogut FAIM MAICD
Chief Executive Officer
Australasian Association of Convenience Stores Limited

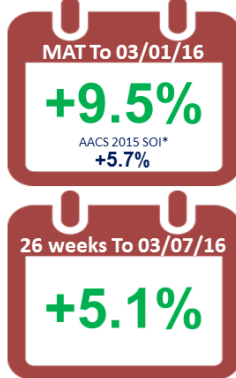
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Appendix

Sub Value Cigarettes continue to grow rapidly as price conscious smokers trade down



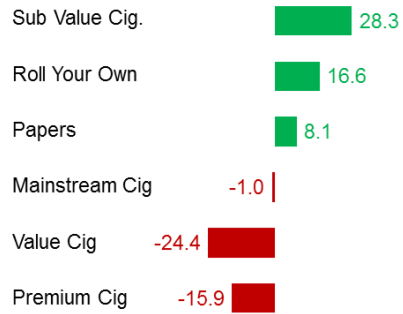
TOBACCO GROWTH
Value Growth %



* Value from the AACs SOI 2015 report using Total Market projected value, based on scan and retailer survey contributions.

TOP AND BOTTOM 3 TOBACCO VALUE DRIVING AND DRAINING SEGMENTS**

Value Growth (%), 26 Weeks To 03/07/16



**Segments ranked by Actual Dollar Growth. Based on IRI Convenience scan sales data (Retailers covered: 7 Eleven, APCO, BP, Caltex, Coles Express, Night Owl, Freedom Fuels, Woolworths Petrol)