



25<sup>th</sup> January 2016

## **AACS SUBMISSION**

**Committee Secretary  
Parliamentary Joint Committee on Law Enforcement  
PO Box 6100  
Parliament House  
Canberra ACT 2600  
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### **Re: Inquiry into illicit tobacco**

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

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,

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## 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 2014 according to companies contributing to the *2014 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. The 2015 report is currently being compiled.

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.

Additionally, we are a member of the Council of Small Businesses of Australia.

## 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 Industry<sup>1</sup> 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 KPMG<sup>2</sup> 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.
- 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.

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<sup>1</sup> *The AACS State of the Industry Report 2014*

<sup>2</sup> *Illicit Tobacco in Australia 2015 Half Year Report*, KPMG

As at October 2015, the illicit tobacco market was estimated by KPMG<sup>2</sup> 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*<sup>3</sup>, 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 well 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.

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.

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 has 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 most recent round of 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.

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<sup>3</sup> *The Impact of Plain Packaging on Australian Small Retailers*, Roy Morgan, 2013

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 KPMG<sup>2</sup> 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.

## **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 down, however the dollar value of sales has remained relatively stable, as excessive tax hikes continue to have a significant impact.

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.

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 AACCS, 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.

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,

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