



TOBACCO BLACK MARKET HITS NEW HIGH: KPMG UK REPORT

Tax loss to government estimated at \$1.35 billion

Consumption of illegal tobacco has reached record levels in Australia with a new report revealing increased activity from tobacco smugglers and unscrupulous traders as the cost of legal cigarettes continues to rise.

The *Illicit Tobacco in Australia Full Year 2014 Report* prepared by KPMG LLP in the UK* shows that illegal tobacco represented 14.5% of total consumption, with nearly 2.6 million kilograms of illicit tobacco consumed last year.

The report, prepared for Philip Morris Limited, British American Tobacco Australia and Imperial Tobacco Australia, reveals the tobacco black market has grown by nearly 30% in two years.

Philip Morris Limited Managing Director John Gledhill said the massive growth in illicit tobacco came during a period which saw two 12.5% tobacco excise increases and the implementation of plain packaging in December 2012.

The KPMG report found that cigarettes in Australia are now among the most expensive in the Asia Pacific region, costing about seven times more than in countries like China and South Korea where much of the illegal tobacco is sourced.

The report says illicit tobacco is mainly smuggled into Australia from overseas and sold at much lower prices than legal cigarettes, avoiding tobacco excise tax obligations. As a result, KPMG estimates that if this tobacco had been consumed in the legitimate market it would have represented an excise amount payable to the Australian Government of approximately AUD\$1.35 billion.

“We believe the government’s excessive tobacco regulations are providing incentives for the black market and cost its own Treasury \$1.35 billion in lost revenue at a time when it is under severe fiscal pressure,” Mr Gledhill said.

The price differentials between legal cigarettes and illicit tobacco continues to widen, with the report highlighting that a packet of illegal cigarettes is up to AUD\$10 cheaper than a legal product while loose tobacco or ‘chop chop’ can be more than AUD\$17.50 cheaper.

Although consumption of illegal (contraband and counterfeit) cigarettes fell by 17% in 2014, KPMG found the growth in the tobacco black market was driven by a massive increase in consumption of ‘chop chop’, which grew by 43% last year and now accounts for 54% of total illicit consumption.

‘Chop chop’ is most commonly sold as finely cut loose leaf tobacco in 250 gram to half kilogram amounts or in boxes of 100 pre-rolled tubes with no labelling or health warnings.

Mr Gledhill said retailers can be fined up to AUD\$340,000 for selling tobacco products that breach Federal plain packaging laws, however, despite the growth in the tobacco black market the Department of Health has yet to prosecute anyone.

“As cigarette smuggling continues to grow in Australia, the government must enforce the law and prosecute people caught selling illicit tobacco,” Mr Gledhill said.

“It is also time for the government to reassess regulations like record tax increases and plain packaging which have created the environment for this insidious black market trade.”

Note: A short broadcast quality video showing real illicit tobacco purchases is available on request.

QUICK FACTS

- The volume of illicit tobacco consumption in Australia grew by 7% in 2014 and now represents 14.5% of total tobacco consumption (13.5% in 2013 and 11.5% in 2012) - the highest level on record.
- The total volume of tobacco consumption in Australia was approximately 17.5 million kilograms, of which almost 2.6 kilograms is estimated to be illicit. Had that tobacco been consumed in the legal marketplace, the Australian Government would have received approximately AUD\$1.35 billion in tobacco excise tax.
- Consumption of unbranded loose leaf tobacco (or chop chop) grew by 43% in 2014 and now accounts for 54% of total illicit consumption (1.4 million kilograms in 2014 / 964,000 kilograms in 2013).
- Consumption of illegal (contraband and counterfeit) cigarettes fell by 17% in 2014, largely due to lower volumes from South Korea.
- Cigarette prices in Australia are more than 75% higher than the most expensive non Australasian market. This large price differential between Australia and nearby markets creates smuggling opportunities for those involved in the illicit tobacco market.
- Asian countries including China and South Korea are the primary source of illegal cigarettes. Loose tobacco or 'chop chop' may be grown in Australia but is most commonly smuggled from overseas countries.
- Tobacco tax increases of 12.5% were imposed in December 2013 and September 2014. Two further 12.5% tax increases are planned for 2015 and 2016. Plain packaging for all legal tobacco products was implemented in December 2012.

* Notes to editors

KPMG UK undertakes economic analysis, commissioned by the tobacco industry, in a variety of jurisdictions. The OECD considers the methodology of KPMG UK the "most authoritative assessment of the level of counterfeit and contraband cigarettes" in the EU. The 'Illicit Tobacco in Australia' report was prepared by KPMG LLP in the UK and is an independent piece of work which gives a reliable insight into the level of illegal tobacco consumption. It was commissioned by BATA, Phillip Morris Limited and Imperial Tobacco Australia. KPMG UK recognises the wider public policy context within which governments decide regulatory and fiscal changes for the tobacco industry, and that the analysis in this report only considers one aspect. KPMG UK expresses herein no view, nor makes any recommendation, in relation to future policy for the industry in this regard.