



12th September 2016

The General Manager
Adjudication Branch
Australian Competition and Consumer Commission
GPO Box 3131
CANBERRA ACT 2601
adjudication@acc.gov.au

AACS submission re: British American Tobacco Australia Limited & Ors application for authorisation A91550

To whom it may concern,

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 Australian Competition and Consumer Commission (ACCC) on the application for authorisation received from British American Tobacco Australia Limited, Imperial Tobacco Australia Limited, and Philip Morris Limited.

This authorisation enables an arrangement between the Applicants to work together to identify, issue warning notices and, if warning notices are not heeded, suspend or cease supply of their tobacco products to retailers and wholesalers who sell illicit tobacco products.

The AACCS strongly supports this application for authorisation. More than simply a positive move, such an arrangement is an absolute necessity.

The only anti-competitive impacts of this arrangement would be felt by rogue retailers who deal with criminal gangs to sell illegal, non-compliant products – and avoid paying the rightful excise on tobacco as a result.

For consumers, an arrangement of this nature cannot come soon enough – for reasons of both fairer competition and basic safety.

Criminal gangs have very effectively filled the market for traditional tobacco products since the introduction of plain packaging and the regular excise increases on legal tobacco.

Illicit tobacco products are by their very nature non-compliant with safety and quality standards and those who sell these products do not do so responsibly. The greater proportion of illicit tobacco of the total tobacco market, the greater chance these non-compliant products will end up in the possession of minors.

Application for authorisation A91550 is an important component of a coordinated approach required, from Government, industry and law enforcement authorities, to crack down on the illicit tobacco market in Australia.

The AACS welcomes the opportunity to be involved in the adjudication process in whatever capacity the ACCC deems fit. Please don't hesitate to contact me should you require anything further.

Jeff Rogut FAIM MAICD
Chief Executive Officer

Australasian Association of Convenience Stores Limited

ACN: 156 638 023

Mobile: 0467 873 789

Office: 03 9807 5552

email: jeff@aacs.org.au

Website: www.aacs.org.au

Mail: PO Box 2309,
Mt Waverley,
Vic. 3149
Australia

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

In this submission the AACS highlights the prevalence of illicit tobacco in Australia, the impact of this illegal market on the convenience industry, and its reasons for supporting the application for authorisation.

Below is a snapshot of the status of the legal and illegal tobacco markets from the convenience industry perspective.

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

AACS strongly supports the authorisation application

The AACS believes authorisation will be of public benefit and will have no negative impacts on competition in the legal tobacco market.

The proposed arrangement has the potential to reduce the amount of illicit tobacco contributing to the total tobacco market. It will also increase the likelihood of retailers and wholesalers caught selling illegal tobacco products to face penalties.

Illicit tobacco is by its very nature non-compliant with safety and quality standards and is much more likely to end up in the possession of minors. Therefore the public benefit is clearly served by the authorisation from the Applicants being granted.

¹ *The AACS State of the Industry Report 2015*

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

The AACS believes there are no negative impacts on competition in the authorisation being granted.

The Applicants themselves are otherwise in direct competition in the legal tobacco market. Only the criminals involved in the production, smuggling and distribution of illicit tobacco, as well as the retailers and wholesalers who sell these illegal products, stand to lose out.

The illicit tobacco market in Australia

The latest independent research from KPMG into black market tobacco consumption in Australia shows that illegal tobacco represented 14.3% of total consumption as at October 2015. Sold legally, this would have generated an extra \$1.42 billion in tax revenue for the Australian Government.

It robs honest retailers of legal tobacco sales. Responsible retailers of legal tobacco are bearing the brunt while the illegal tobacco market has grown significantly in recent years.

It is a disturbing trend that demonstrates the unintended consequences of poorly planned Government policy, as the criminals who supply these illegal tobacco products don't care if it ends up in the hands of minors. There are also no quality checks on what is actually in the products.

The Australian regulatory environment continues to contribute to our growing reputation as one of the world's most lucrative markets for illegal tobacco.

Legal tobacco remains an important product for small businesses and the more the market for illicit tobacco expands, the more these small businesses will suffer. Consider the quote below from an actual retailer – and small business owner – on the impact of illicit tobacco on a typical convenience store:

***“My conservative estimates are that illicit tobacco is costing my business at least \$200 per day in tobacco and associated sales. My decline in customer count traffic commenced when the (nearby) illegal outlet opened in February this year.*”**

“Not only is this having an adverse effect on my business profitability, but it's also costing [brand withheld] Service Stations nearly \$10K per year in lost revenue and supplier rebates.”

The point is clear: the illicit trade of tobacco is having a pronounced negative impact on small businesses around Australia. Illicit tobacco is widely and readily available through many unscrupulous sources. The need to target the illicit tobacco market is urgent.

Targeting the illicit tobacco market

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

A coordinated effort to crack down on the illicit trade of tobacco is perhaps the most obvious and effective measure to reduce the incidence of smoking, particularly among minors, while ensuring those who are licensed to sell a legal product are not negatively impacted.

The authorisation is one component of the coordinated approach required.

A hotline for retailers and consumers to alert authorities to the illicit trade of tobacco could also 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 in targeting the criminals involved in the illicit market.

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 in the illicit tobacco market 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 AACCS 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.

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

The effectiveness of existing 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 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.

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.

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.

Conclusion

The AACS, as the representative and voice for convenience stores across the country, emphasises 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 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.

The AACS believes a coordinated effort from Government, industry and law enforcement authorities is necessary to effectively crackdown on the illicit tobacco market in Australia.

The application for authorisation is a key component of the coordinated effort required and the AACS therefore strongly supports the application.

Thank you for your consideration of our submission.

Jeff Rogut FAIM MAICD
Chief Executive Officer
Australasian Association of Convenience Stores Limited
ACN: 156 638 023

Mobile: 0467 873 789
Office: 03 9807 5552
email: jeff@aacs.org.au
Website: www.aacs.org.au

Mail: PO Box 2309,
Mt Waverley,
Vic. 3149
Australia