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Dear Hannah

Response to submissions - A91550

Thank you for inviting us (on behalf of the Applicants) to respond to submissions made with respect to application for authorisation A91550.

The Applicants are pleased to note that the majority of submissions by interested parties are made in support of the application. In particular, the Applicants note strong support from a range of retailers and retailer associations and their views that the proposed conduct would provide a benefit to retailers and consumers.

This letter responds to key issues raised in the submissions. Specific matters raised in particular submissions are also addressed by this letter.

This letter is for the public register.

1 Executive summary

- 1.1 Following a review of submissions that oppose or do not support the application, the Applicants do not consider that those submissions raise any matters that would outweigh the public benefits of granting the application.
- 1.2 Several submissions refer to Article 5.3 of the World Health Organisation Framework Convention for Tobacco Control (**WHO FCTC**). The Applicants note that Article 5.3 specifies transparency in dealings between governments and the tobacco industry. The Applicants submit that this authorisation process clearly satisfies that requirement, as does the conduct proposed in the application. Aside from matters of transparency, Article 5.3 is of no bearing to this application.
- 1.3 In addition, the proposed conduct would be performed by the Applicants in their private capacity against private parties. It does not require, contemplate or rely upon any government agency involvement. To equate the proposed conduct as amounting to a form of 'law-enforcement' is an incorrect description of the proposed conduct and the Applicants' rights at law. The Applicants consider it is very important that the ACCC notes this distinction in considering the application.

- 1.4 The Applicants already have private rights and remedies to independently conduct mystery shopper purchases and cease supply, including due to breach of a contract made between any of the Applicants and a retailer or wholesaler. The relevant distinction between that conduct and the conduct proposed in the application is that the Applicants wish to coordinate their conduct so as to close-out an existing loop-hole whereby retailers found to be selling illicit tobacco switch from one Applicant to another to ensure a continued supply of legal tobacco products.
- 1.5 The Applicants note that some of the submissions questioned the proposed levels of transparency and reporting. In this letter, the Applicants propose additional steps that they are willing to take to address these concerns, even though they are not considered necessary given the protections already put into the process for identifying and dealing with illicit products (as originally proposed in the supporting submission to the application).
- 1.6 Given the very low risk of any lessening of competition as a result of the proposed conduct, the Applicants submit that the public benefits of the limited and evidenced-based conduct proposed in the application far outweigh any potential detriments to the public.
- 2 Article 5.3 - WHO Framework Convention for Tobacco Control**
- 2.1 Article 5.3 of the WHO FCTC states that “[i]n setting and implementing their public health policies with respect to tobacco control Parties shall act to protect these policies from commercial and other vested interests of the tobacco industry in accordance with national law” (emphasis added with underline).
- 2.2 Examples of these public health policies are set out in the WHO FCTC and include price and tax measures, measures to protect people from exposure to tobacco smoke and regulation of tobacco products.
- 2.3 Certain submissions to the ACCC raise Article 5.3 of the WHO FCTC.
- 2.4 Those submissions include (in summary):
- (a) Cancer Council Victoria considered that, given Article 5.3, it would not be appropriate for there to be a perception of government being in partnership with the tobacco industry;¹
 - (b) Cancer Council Western Australia considered that the application would ‘breach’ Article 5.3;² and
 - (c) the WA Minister for Health, Culture & the Arts considered that the WHO FCTC sets out a need to protect tobacco control from industry interference.³
- 2.5 While the submission made by the federal government agency responsible for implementing health policies on tobacco control (the Commonwealth Department

¹ Cancer Council Victoria, p. 3.

² Cancer Council Western Australia, p. 2.

³ Minister for Health, Culture & the Arts, Government of Western Australia, p. 1.

- of Health) discusses Article 5.3 and other matters for consideration by the ACCC, the Department of Health submission does not oppose or support the application.
- 2.6 The Applicants note that the Department of Health, the Department of Immigration and Border Protection and the Australian Tax Office have for some time communicated with representatives of the tobacco industry (including with representatives of the Applicants). The forums and/or government agencies for such cooperation with respect to the trade in illicit tobacco include:
- (a) the Department of Immigration and Border Protection:
 - (i) Industry Advisory Group - Policy Group subcommittee;
 - (ii) Industry Advisory Group - Operational Group subcommittee; and
 - (b) the Australian Tax Office Tobacco Stakeholders Group for which minutes are published by the ATO.⁴
- 2.7 Relevantly, much of the communication and cooperation between representatives of the tobacco industry and relevant government agencies is directed at reducing the trade in illicit tobacco.
- 2.8 For example, a government agency may seek the assistance of one or more of the Applicants to determine whether a suspected product being investigated by the government agency is a lawful product of one of the Applicants or, alternatively, counterfeit.
- 2.9 It is also noted that industry engagement is a key strategy of the Department of Immigration and Border Protection. Its 'Industry Engagement Strategy 2020' *"reaffirms [its] commitment to working with industry in strategy, forward-focussed partnership"*.⁵
- 2.10 In addition, to assist with law enforcement, the Applicants voluntarily report contraventions of tobacco control laws to government agencies, including reporting contraventions to the Department of Health, the Department of Immigration and Border Protection and the Australian Tax Office.
- 2.11 Importantly, while the guidelines to Article 5.3 of the WHO FCTC note that there is a conflict between the tobacco industry's interests and public health policy interests, in the specific case of combating illicit tobacco, the interests of industry and government are aligned. They have the same objective of reducing the availability and supply of illicit tobacco to consumers.
- 2.12 An important consequence of this alignment is that the risks with which Article 5.3 is concerned are not, in the Applicants' opinion, relevant to the proposed conduct.
- 2.13 The Applicants and interested parties all agree that the availability and supply of illicit tobacco products undermines existing tobacco control measures.
- 2.14 In addition:

⁴ See < <https://www.ato.gov.au/general/consultation/consultation-groups/stakeholder-relationship-groups/tobacco-stakeholder-group/> >

⁵ Department of Immigration and Border Protection, Industry Engagement Strategy 2020 (Trade, Customs and Traveller) (2015), p. vi.

- (a) Article 5.3 requires transparent dealings between government agencies and the tobacco industry and this public application process meets that requirement; and
 - (b) the Applicants are not asking for any change in health or any other government policy, they are simply applying for authorisation to exercise individual contractual remedies in a coordinated manner.
- 2.15 Any reduction in the availability of illicit tobacco through the proposed conduct will, among other benefits, support the awareness of health warnings applied to the Applicants' regulated and lawful products, which are generally not applied to illicit tobacco products.
- 2.16 Finally, the primary objective of Article 5.3 (which is, in the Applicants' view, to prevent the tobacco industry from detrimentally influencing the setting or implementation of public health policies with respect to tobacco control) is not something that could arise from the proposed conduct for the following reasons:
 - (a) the proposed conduct does not involve any conduct that would or could influence policy making, on the contrary, the proposed conduct of the Applicants is likely to give better effect to tobacco control measures by reducing the level of illicit tobacco products, which are not subject to those control measures;
 - (b) the proposed conduct would be performed by the Applicants in their private capacity against private parties, it does not require, contemplate or rely upon any government agency involvement;
 - (c) any conditions of authorisation (such as those proposed by the Applicants in this letter) that may require reporting by the Applicants to relevant government agencies would be in accordance with such conditions and would be limited to reporting activities, not activities designed to influence public health policy in any way; and
 - (d) from an implementation perspective, and taking into account that most illicit tobacco is imported into Australia:
 - (i) the Department of Immigration and Border Protection does not oppose the application and states that "*The application does not impact directly on border controls, legislation or activities*";⁶ and
 - (ii) the Department of Health does not provide any examples of how the exercise of the Applicants' private rights (which they already may exercise independently of each other and which would not materially change by the coordinated exercise of those rights by the Applicants) would interfere with investigations being conducted by law enforcement.

Claims of partnership between the Applicants and government

⁶ Department of Immigration and Border Protection submission (4 November 2016).

- 2.17 Cancer Council Victoria submitted that, should the application be authorised, it should be conditional upon the Applicants refraining from making any representation or engaging in conduct which is capable of giving retailers, wholesalers or members of the public the impression that the Applicants are in any way working in collaboration or partnership with the ACCC, the ATO or the DIBP Tobacco Strike Team.
- 2.18 It is unrealistic to claim that the particular conduct proposed by the application will create a perception of a partnership between government and the Applicants. This is an application to allow the Applicants to coordinate conduct that each of them already have a right to engage in independently to combat and discourage the supply of illegal tobacco by retailers and wholesalers.
- 2.19 Nothing in the application proposes that government, or any agency of government, partner or become actively involved with the Applicants in the proposed conduct, though the Applicants note that a number of submissions recommend reporting by the Applicants to relevant government agencies. Reporting is something that the Applicants are more than happy to consider and would be consistent with their existing cooperation and communication with government agencies about the trade in illicit tobacco.
- 2.20 The Applicants are subject to the laws with respect to misleading or deceptive conduct and are very mindful of their obligations under those laws. As such, they would not improperly represent the nature of their activities when dealing with retailers, wholesalers or members of the public with respect to the proposed conduct. Should the ACCC consider that an additional condition would be appropriate, the Applicants are willing to consider such a condition (or clarifying statement) that would be communicated as part of performing the proposed conduct.

3 Transparency and reporting

- 3.1 Certain submissions raised issues regarding transparency, monitoring, reporting and decision-making. Those issues include:
- (a) Cancer Council Victoria considered that:
 - (i) the proposed arrangements lacked transparency, including that the Applicants were not required to provide any information to the ACCC or other government departments/agencies regarding any illicit tobacco sales detected, or any action taken by the Applicants as a result of such detection;⁷ and
 - (ii) should the application be authorised, Applicants should be required to report to agencies on a regular basis.⁸
 - (b) MGA Independent Retailers submitted that the Applicants should be required to “*pass on any information collected regarding illicit tobacco to the relevant authorities for further investigation*”;⁹ and

⁷ Cancer Council Victoria, p. 3.

⁸ Cancer Council Victoria, p. 5.

(c) the Department of Health noted its concerns with “*consistency, transparency and accountability*” under the process.¹⁰

3.2 The Applicants reject that the proposed arrangement lacks transparency. The arrangement is the subject of a public authorisation process and is appropriate given that it primarily involves the exercise of private rights by the Applicants. To the extent that the process involves the Applicants exercising private rights, it is not appropriate for all aspects of the process to be public.

3.3 As noted under heading 2 of this letter, the Applicants already engage in appropriate cooperation and communication with a variety of government agencies for the purposes of combating the trade in illicit tobacco.

3.4 The Applicants are willing to continue that cooperation and communication, including reporting suppliers of illicit tobacco identified by them to relevant government agencies in a manner that is consistent with their existing levels of reporting of illicit tobacco to government agencies.

4 Appeals process

4.1 The Australian Lottery and Newsagents’ Association (**ALNA**) submitted that an appeals mechanism should be available to retailers.¹¹

4.2 The ALNA provided some suggestions on how such an appeals mechanism could operate including that it be formed of “*three members, one from the tobacco companies, one from the retailers and an independent chair*”, and that its decisions be binding.¹²

4.3 The Applicants do not consider that the joint exercise of their private rights or the conduct that is proposed to be authorised should include any independent appeals process. The proposed conduct already involves an opportunity for the relevant retailer or wholesaler to respond to evidence presented to them by the Applicants.

4.4 It must also be remembered that the Applicants propose to exercise their private rights. The exercise of those private rights is not currently subject to any bespoke appeals process other than the usual actions that would be available to an aggrieved retailer or wholesaler to seek relief through existing arbitration provisions in their contracts with the Applicants or, where applicable, through the courts.

5 Period of authorisation

5.1 The Applicants seek authorisation for a limited period of 5 years.

5.2 Cancer Council Victoria proposed that, if the arrangement is authorised, the arrangement should be subject to review by the ACCC in two years “*in order to*

⁹ MGA Independent Retailers, p. 3.

¹⁰ Department of Health, p. 7.

¹¹ Australian Lottery and Newsagents’ Association, p. 1.

¹² Australian Lottery and Newsagents’ Association, p. 1.

allow an opportunity to identify and address any problems with the arrangement. The review should involve public consultation with interested parties.”¹³

- 5.3 The requirement for a review to be undertaken by the ACCC was also raised in other submissions.
- 5.4 The Applicants do not oppose a review of the provisions being undertaken but do not agree that a review would be warranted after just two years.
- 5.5 It is noted that the submission from Professor Davidson also suggested a review of the proposed conduct could be implemented in lieu of on-going monitoring *“after a reasonable time period has elapsed (say five years)”*.¹⁴ Such a proposal is consistent with the five year period of authorisation requested by the Applicants.
- 5.6 Given that additional monitoring and reporting has already been proposed, and the application for authorisation is only for a limited period of five years, the Applicants do not consider that a further review within the five-year period would be efficient or warranted.
- 5.7 It would be appropriate for the ACCC, other government agencies, the industry and other interested parties to reassess the arrangements at the end of the five year authorisation period. A five year authorisation period would allow sufficient time to have passed to determine the effectiveness of the process and to measure the impact of the conduct on the trade in illicit tobacco.

6 Interaction with law enforcement activities

- 6.1 The Western Australia Minister for Health, Culture & the Arts considered that the application poses *“significant inherent conflict”* for the tobacco industry to be involved in enforcement activity related to tobacco control.¹⁵
- 6.2 The Department of Health submitted that *“[t]he quasi law-enforcement activities that the Applicants wish to undertake may interfere with investigations being conducted by law enforcement”*.¹⁶ The Department of Health does not provide any examples of how the exercise of the Applicants’ private rights (which they already may exercise independently of each other and which would not materially change by the coordinated exercise of those rights by the Applicants) would interfere with investigations being conducted by law enforcement.
- 6.3 The Applicants submit that it is incorrect and misleading to conflate the lawful, contractually-based civil arrangements proposed by the Applicants with civil and criminal law enforcement activities of government agencies and, on that basis, to assert, albeit in very general terms, that the former may somehow undermine the latter.
- 6.4 Under the proposed conduct, the Applicants would adopt an evidenced-based approach to enforce, in a co-ordinated manner, contractual rights that each of the

¹³ Cancer Council Victoria, p. 5.

¹⁴ Sinclair Davidson, p. 9.

¹⁵ Minister for Health, Culture & the Arts, Government of Western Australia, p. 1.

¹⁶ Department of Health, p. 7.

- Applicants can currently enforce individually in accordance with their respective commercial contracts and trade terms with retailers of legal tobacco products.
- 6.5 Such conduct would not amount to “*quasi-law enforcement activities*” and would not replicate or undermine any action by a law enforcement agency such as the Australian Taxation Office or the Australian Border Force could undertake.
- 6.6 As outlined in the application, and agreed by a number of submissions, any action taken pursuant to the proposed conduct (if authorised) would complement the efforts and objectives of law enforcement agencies, not work against them.
- 6.7 Dr John Coyne’s submission noted that, while enforcement agencies will play an important role, the application represents proactive steps that the Applicants can take as an industry.¹⁷
- 6.8 The Applicants submit that the proposed arrangements should have positive direct effects by tackling the sale of illicit tobacco at the retail level. It should also assist, in parallel with law enforcement activity, in effectively deterring others from engaging or continuing to engage in the trade of illicit tobacco products.
- 6.9 Given the proposed arrangements, and any additional reporting requirements as discussed above, the Applicants consider that an evidence-based process and transparent reporting will help ensure that there are no conflicts within the regulatory framework.
- 6.10 The Applicants acknowledge the important role that law enforcement agencies play in combating the trade in illicit tobacco. As set out in the supporting submission to the application, law enforcement efforts to date have been focused on illegal activities occurring much higher in the illicit supply chain. Commonwealth agencies have openly acknowledged that successful investigation and prosecution at the retail or wholesale level is difficult.
- 6.11 The application, if granted, would not change or otherwise adversely impact existing government and government agencies’ policies, practices and strategic priorities on tobacco control or law enforcement.
- 6.12 The Applicants note that no examples of how the proposed conduct would have such an impact have been put forward by any of the government agencies that have made submissions.
- 6.13 The benefit that such coordinated action would provide is acknowledged in a number of submissions, including those from Professor Sinclair Davidson,¹⁸ Dr Adam Masters,¹⁹ Cignall,²⁰ and Ritchies Supermarkets and Liquor Stores.²¹

¹⁷ Dr John Coyne, p. 2.

¹⁸ Professor Sinclair Davidson, pp. 6-9;

¹⁹ Dr Adam Masters, p. 3.

²⁰ Cignall, p. 2 where it was submitted the authorisation should be granted to “*allow the three manufacturers to come together and prepare a joint strategy, to enable them to have some impact on the significant quantities of illicit tobacco being sold in Australia*”.

²¹ Ritchies Supermarkets & Liquor Stores, p. 1 where it was submitted that the application had its “*complete endorsement*” for the Applicants to work together.

The submission from Professor Davidson noted “*private enforcement of public rules ... have been shown to be efficient in other industries*”.²²

7 Size of the illicit tobacco market in Australia

- 7.1 Submissions by the Cancer Council Victoria and the Cancer Council Western Australia consider that the size of the illicit market in Australia has been over-stated by the tobacco industry and that there is tobacco industry bias in the report produced by KPMG.²³
- 7.2 In its submission, the Department of Health did not consider that the KPMG report “*provided a reliable estimate of the illicit tobacco market in Australia*”.²⁴
- 7.3 Given their nature, there will always be inherent difficulties in measuring the exact size of all illegal industries. However, what is not in dispute is that the trade in illicit tobacco in Australia has been recognised by government as representing a serious problem in Australia. Clear evidence of this is the initiation of the illicit tobacco inquiry by the Parliamentary Joint Committee on Law Enforcement, which is ongoing and which will be conducting further hearings in Canberra during the week commencing 21 November 2016.
- 7.4 In addition, the Tobacco Strike Team of the Australian Border Force was established in 2015 with additional funding provided in June 2016 to expand the strike team.²⁵
- 7.5 In comments made to a Senate estimates hearing on 23 February 2015, Mr Roman Quaedvlieg, Chief Executive Officer of the Australian Customs and Border Protection Service stated, as part of his answer to a question about what trends he was seeing with respect to illicit tobacco:
- Tobacco is one of our six primary operational priorities that I set in the middle of last year. In the six months of this financial year to date we have 51 active cases of illegal tobacco under investigation. We have made 46 detections of tobacco for some 80 tonnes of loose-leaf tobacco and 20-odd million loose cigarettes. That has a revenue concomitant estimation of around \$52 million. We are seeing an increase in organised crime entities involved in this. I put it down partially to the fact that the excise in duty payable on tobacco is increasing. We are halfway through a four-year incremental increase to a tune of 12.5 per cent.²⁶
- 7.6 Most recently, at the Senates Estimates hearing, the Acting Commissioner of the ABF acknowledged that “*tobacco has become an attractive commodity for serious organised crime*”.²⁷

²² Sinclair Davidson, p. 9.

²³ Cancer Council Victoria, pp. 1-2; Cancer Council Western Australia, p. 2.

²⁴ Department of Health, p. 3.

²⁵ <http://www.minister.border.gov.au/peterdutton/2016/Pages/expansion-abf-tobacco-strike-team.aspx>

²⁶ Official Committee Hansard, Senate, Legal and Constitutional Affairs Legislation Committee Estimates (23 February 2015), page 121.

²⁷ Proof Committee Hansard, Senate Estimates, Legal and Constitution Affairs Legislation Committee, 17 October 2016, p. 85.

- 7.7 In relation to the comments from the Department of Health about the size of the illicit tobacco market, the Applicants note that the application is supported by the KPMG report in addition to the other factors that are outlined in the Application, such as:
- (a) the submissions (over 160) made to the Federal Parliamentary committee;
 - (b) the recognition of the Australian Crime Commission that “*organised crime remains entrenched within the illegal tobacco market in Australia*”;²⁸
 - (c) the on-going recognition by government of the risks posed by the illicit tobacco industry to the community (the Applicants also wish to note that the 14% figure referred to at page 3 of the submission of the Department of Health was the value reported for 2015 (full year) and was not, as claimed by the Department of Health, “*rounded down*”);
 - (d) the evidence submitted by the Australian Institute of Health and Welfare (AIHW) to the Parliamentary Joint Committee on Law Enforcement on 4 March 2016 that the approach used by KPMG to estimate the size of the illicit market was “*probably the most appropriate way to measure this type of information*”²⁹; and
 - (e) when asked about the methodology of the KPMG Report, the AIHW representative noted that they “*do not really have any criticisms*” of the KPMG report’s methodology and that the consumer survey data comes from a trustworthy source (being Roy Morgan, which also undertakes the AIHW research that is referred to by the Cancer Councils and the Department of Health).³⁰
- 7.8 The Department of Health submitted that it considers there needs to be a robust estimate of the size of the illicit market and that it “*supports the work of DIBP and ATO in developing more accurate models to estimate the size of the illicit tobacco market*”.³¹
- 7.9 The Applicants welcome developments of new methods to estimate the size of the illicit tobacco market. However, in the interim, the Applicants submit that the KPMG report provides a proven methodology, which has been acknowledged by AIHW as “*probably the most appropriate way to measure this type of information*” (as noted above in paragraph 7.7(d)).³²
- 7.10 The Applicants also note that there is no disagreement between the Applicants and any interested party that a trade in illicit tobacco works against tobacco control measures in Australia.

²⁸ Australian Crime Commission, *Organised Crime in Australia* (2015), p. 68.

²⁹ Official Committee Hansard, Parliamentary Joint Committee on Law Enforcement, *Illicit tobacco*, 4 March 2016, p. 33.

³⁰ Official Committee Hansard, Parliamentary Joint Committee on Law Enforcement, *Illicit tobacco*, 4 March 2016, p. 33.

³¹ Department of Health, p. 4.

³² Official Committee Hansard, Parliamentary Joint Committee on Law Enforcement, *Illicit tobacco*, 4 March 2016, p. 33.

8 Compliance and evidence-based approach

- 8.1 Cancer Council Victoria claim that studies have shown that there is no evidence of any increase in use of illicit tobacco following the introduction of plain packaging.³³
- 8.2 The Department of Health also submitted that “[t]here is no reliable evidence that plain packaging has had any effect on the illicit tobacco market”.³⁴
- 8.3 The Applicants note that Cancer Council Victoria referred to two consumer surveys undertaken in the 2012 to March 2014 period on illicit tobacco use in Victoria and Australia wide. As discussed above, since the completion of these surveys, the impact, size and nature of illicit tobacco market in Australia has been recognised by government.
- 8.4 The Applicants also note that the KPMG report found an increase in illicit volumes (and therefore usage) from 2.0 million kg in 2012 to 2.5 million kg in mid-2014.³⁵ The report found that the key driver of this change was the proliferation of contraband (branded cigarettes) as measured by the Empty Pack Survey, which grew from 0.5 million kg to 1.3 million kg. The Empty Pack Survey is based on physical, actual packs collected around key population centres Australia-wide.³⁶
- 8.5 The Department of Health submitted that “[n]on-compliance with tobacco plain packaging does not necessarily mean that a product is illicit” and questioned “how will the Applicants determine if a product is illicit”.³⁷ The Department’s comments are surprising. Any product that is counterfeit or does not meet the requirement of Australian laws and regulations, including the provisions under the plain packaging legislation is illicit. The WHO FCTC defines “illicit trade” to mean “any practice or conduct prohibited by law and which relates to production, shipment, receipt, possession, distribution, sale or purchase including any practice or conduct intended to facilitate such activity”.³⁸
- 8.6 There are a range of forensic means available to establish whether a product is in fact illicit, such as verifying if product sold in retail channels is in plain packaging and contains Australian health warnings or by expert analysis of the packaging in the case of counterfeiting. These techniques are commonly used, evidence-based and would be applied by the Applicants in determining whether a particular covert mystery shopper purchase is illicit.
- 8.7 The intent of the Applicants would be that evidence collection, examination and testing of products would be performed to a standard necessary for such evidence to be admitted in court.
- 8.8 Importantly, the Applicants have no motivation to falsely claim that a product acquired through mystery shopper purchase is illicit when it is not. Such conduct would be unlawful and would materially damage the reputation of the Applicants.

³³ Cancer Council Victoria, p. 2.

³⁴ Department of Health, p. 5.

³⁵ KPMG LLC, Illicit tobacco in Australia, 2015 Full Year Report (15 April 2016), 6.

³⁶ Additional details on the Empty Pack Survey can be found in the KPMG reports on illicit tobacco in Australia, including the latest version provided with the application.

³⁷ Department of Health, p. 7.

³⁸ WHO FCTC, Article 1.

A determination that a product is illicit would only be made where the evidence is clear that it is in fact illicit and the reasons why it is illicit.

- 8.9 In addition, as noted under heading 8 of the supporting submission of the Applicants dated 25 August 2016, it is clearly not in the interests of the Applicants to target retailers or wholesalers of legal tobacco products who do not acquire or sell illicit tobacco products. To do so would affect the sale of the legal tobacco products of the Applicants and damage the valuable commercial relationship that exists between the Applicants and the retailers and wholesalers of legal tobacco products in Australia.

9 Excise

- 9.1 The Department of Health submission refers to a 2007 study by the World Health Organisation that considered countries with lower tobacco prices tended to have larger illicit tobacco markets. The Department considered this study is contrary to the concerns raised in the application on the impacts of increasing excise on increasing illicit tobacco.³⁹
- 9.2 The study referenced by the Department uses figures from 2007, which presented averaged data across a number of jurisdictions. In many of the regions included in the study, there are significant differences in the legal and political landscape, rendering those comparisons and inappropriate.
- 9.3 Given the significant differences between jurisdictions, and the age of the analysis, the Applicants do not consider that comparisons of broad averages in this instance provides useful information for the assessment of this application. As noted by the Department, there are various factors that impact the illicit market in addition to price.
- 9.4 A key factor for consideration is the potential profitability of illicit tobacco, which is high in Australia. As acknowledged by the Australian Crime Commission, the illegal tobacco market in Australia is “a low risk, high profit enterprise”.⁴⁰
- 9.5 In addition, as noted by the Department, other factors influencing illicit trade include the existence of distribution networks, elements of organised crime and corruption, likelihood of detection and the scale of penalties. As is discussed in detail in the supporting submission to the application, the Applicants note that organised crime has been found to be operating in the illicit tobacco market in Australia.
- 9.6 The Department of Health submitted that the Applicants were “*circumspect regarding the precise benefit*” of the application and the Department also noted that “*it is not necessarily the case that any reduction in illicit tobacco would translate to an equivalent increase in licit tobacco use and government revenue*”.⁴¹
- 9.7 As acknowledged in the application, the Applicants accept that, given the nature of illicit trade, the benefits of the proposed conduct, if authorised, would be difficult to precisely calculate. Nonetheless, based on seizures of illicit tobacco products

³⁹ Department of Health, pp. 4-5.

⁴⁰ Australian Crime Commission, *Organised Crime in Australia* (2015), p. 68.

⁴¹ Department of Health, p. 4.

alone in 2015, more than \$60 million in street value of illicit tobacco products were seized by authorities.

- 9.8 The authorisation, if granted, it would only need to have a small impact to lead to a significant reduction in proceeds to organised crime, thereby providing a public benefit. Finally, the public benefits of the proposed conduct are not limited to potential increases in excise revenue to government. There are a range of other very significant public benefits, as described in more detail in the supporting submission to the application.

10 Government reviews

- 10.1 The Department of Health and the DIBP both noted that review of legislative arrangements to strengthen arrangements around illicit tobacco are ongoing.⁴² The DIBP submitted that “[s]ome of these inconsistencies and enforcement shortcomings are, however, being addressed by the Australian Government”.⁴³

- 10.2 In its recent Industry Summit communiqué dated 31 October 2016, the DIBP stated:

The Summit focused on the partnerships that make this possible, the ways we can strengthen them, and the border solutions we can forge together in order to seize opportunities for mutual benefit and to build Australia’s future.

This year’s Summit explored how the Department and industry could work together to improve the trade and travel experience, comply with our border obligations, and support regional Australia. Workshops and panel discussions were structured in such a way to allow delegates to actively participate and provide innovative ideas for the future.

It is through the unique partnerships we are building with Australian businesses, and across the breadth of industries they represent, that we forge a strong Australian community and a prosperous, competitive economy.⁴⁴

- 10.3 The Applicants welcome the DIBP’s acknowledgement of existing enforcement issues across the various agencies involved.
- 10.4 The current inconsistencies and shortcomings reinforce the likelihood of the application providing public benefits. Changes to the law may take some time and, once implemented may not be effective or may be affected by the level of resources available to relevant government agencies to implement and enforce those laws.
- 10.5 The conduct proposed in the application would provide an additional and immediate means based on the exercise of private rights, to disrupt the supply of illicit products to consumers.

⁴² Department of Health, p. 3; Department of Immigration and Border Protection, p. 1.

⁴³ Department of Immigration and Border Protection, p. 1.

⁴⁴ Industry Summit communiqué (31 October 2016)

< <http://www.border.gov.au/Engagingwithindustry/Documents/industry-summit/industry-summit-communique.pdf> >

11 Supply of illicit products through existing retailers

- 11.1 The Department of Immigration and Border Protection submission included a correction in an apparent inaccuracy in the application where it was stated that the DIBP research reveals that “*most of*” the illicit trade is conducted through existing retailers.
- 11.2 The Department noted that although it had stated “*illicit tobacco is available from a number of traditional tobacconists and tobacco retailers, it has not commented on, and is unable to comment on, the proportion of illicit trade that is conducted through existing retailers*”.⁴⁵
- 11.3 The Applicants thank the Department for this clarification. The Applicants note that the research undertaken by Roy Morgan for the KPMG Report has found that the majority of illicit products are purchased through existing retailers.

12 Providing information to retailers

- 12.1 Cancer Council Victoria proposed that, if the arrangement is authorised, retailers should be clearly informed about the arrangement and should be encouraged to raise any concerns with the ACCC.⁴⁶
- 12.2 In response to this the Applicants note the following:
- (a) this application is a public process;
 - (b) Cancer Council Victoria does not represent retailers;
 - (c) retailers have already made submissions substantially in support of the proposed conduct; and
 - (d) as is documented in the proposed conduct, if a retailer is trading in illicit tobacco, it will receive direct notification from the Applicants advising them of the steps that will be taken.

13 Minor tobacco brands

- 13.1 The Department of Health also contends that “[t]here is a clear conflict of interest regarding the business interests of the Applicants and other minor tobacco brands which may form part of the licit market”.⁴⁷ The Department does not explain the nature of the conflict or provide any examples of how the conflict may manifest itself.
- 13.2 The Applicants disagree that there would be negative competitive impacts on the minor licit brands. The Applicants would only target retailers selling illicit brands. This activity is likely to support minor tobacco brands because they will, to the extent that the retailer/wholesaler ceases its acquisition and resupply of illicit tobacco, benefit from not having to compete with illicit tobacco products previously being sold by that retailer/wholesaler, and yet would not have incurred the cost or effort of the Applicants in achieving such a result.

⁴⁵ Department of Immigration and Border Protection, p. 1.

⁴⁶ Cancer Council Victoria, p. 5.

⁴⁷ Department of Health, p. 7.

13.3 In addition, any decision by the Applicants to cease supply to a particular retailer would not prevent that retailer from acquiring legal tobacco products from a minor tobacco brand (the proposed conduct is limited to the legal tobacco products of the Applicants).

14 Increased supply of illicit tobacco

14.1 Cancer Council Victoria submitted that the covert mystery shopper approach may give retailers the impression that demand for illicit products has increased and therefore result in increased supply of illicit products.⁴⁸

14.2 The Applicants reject this claim. Mystery shopper activity would not be conducted at such a frequency to create an artificial increase in demand for illicit tobacco products. Total illegal tobacco is estimated to be worth around \$1.49bn per annum.⁴⁹ Any mystery shopper activity would therefore be insignificant in creating any impressions about the trade in illicit tobacco, particularly compared to other activities, such as press coverage of law enforcement successes.

14.3 Cancer Council Victoria also submitted that the proposed arrangement could result in an increase in awareness, and therefore demand for, illicit tobacco products from the public if the Applicants make any public statements about the proposed arrangements.⁵⁰

14.4 The Applicants consider that:

- (a) it is important to increase public awareness of the dangers associated with, and the negative impacts of purchasing illicit products and the links of illicit tobacco to other criminal activities;
- (b) there needs to be greater awareness that consumers purchasing illicit products (and the suppliers of those products) are breaking the law;
- (c) there needs to be a reduction in the community's tolerance for the trade in and availability of illicit tobacco products; and
- (d) this will not change the rights currently available to the Applicants individually or jointly to engage in public awareness campaigns.

14.5 The trade in illicit tobacco products has the potential to cause further damage to the community generally, including that the illicit tobacco trade funds other organised crime.

14.6 Educating the public has been an important consideration in other jurisdictions, such as in the UK where changing public perception and reducing tolerance of fraud is a key component of the Her Majesty's Revenue & Customs tackling illicit tobacco strategy.⁵¹

14.7 Finally, the Applicants consider that consumer awareness has been increasing following the establishment of the Tobacco Strike Team of the Australian Border Force and the success that the team has had in combating illicit tobacco.

⁴⁸ Cancer Council Victoria, p. 4.

⁴⁹ KPMG LLC, Illicit tobacco in Australia, 2015 Full Year Report (15 April 2016), 6.

⁵⁰ Cancer Council Victoria, p. 4.

⁵¹ HM Revenue & Customs and Border Force, Tackling illicit tobacco: From leaf to light, 24 March 2015.

15 Conclusion

- 15.1 In this letter, the Applicants have addressed key issues of concern raised by submissions which oppose or do not support the conduct proposed in the application.
- 15.2 The arguments put forward in this letter challenge claims made in some of the submissions, including with respect to:
- (a) incorrect assumptions that there should be no cooperation or communication between the tobacco industry and government agencies responsible for targeting illicit tobacco;
 - (b) incorrect conclusions that the interests of the Applicants conflict with those of government agencies with respect to the proposed conduct (when in fact they are aligned when it comes to reducing illicit tobacco);
 - (c) incorrect claims that the proposed conduct (which involves the exercise of private rights) is a form of law enforcement that would overlap or interfere with the activities of law enforcement agencies; and
 - (d) incorrect claims that the process proposed by the Applicants is not evidence-based or is lacking in transparency or integrity.
- 15.3 In this letter, the Applicants have also expressed their willingness to agree to measures such as appropriate reporting to relevant government agencies and to discuss such proposals in any conference that may occur.
- 15.4 In conclusion, the Applicants submit that the extensive public benefits of the proposed contract, and arrangement between them, significantly outweigh any potential public detriment.

16 Further information

- 16.1 Thank you for the opportunity to respond to submissions made.
- 16.2 The Applicants are happy to meet with the ACCC if you have any issues you wish to discuss in further detail.
- 16.3 Please contact me if you have any queries or require further information.

Yours faithfully
Corrs Chambers Westgarth



Eddie Scuderi
Partner