

NATIONAL
COALITION
AGAINST
CONTRABAND
TOBACCO

Stopping the sale of illegal cigarettes in Canada



LA COALITION
NATIONALE
CONTRE
LE TABAC DE
CONTREBANDE

Enrayer la vente de cigarettes illégales au Canada

National Coalition Against Contraband Tobacco 2017 Pre-Budget Recommendations

About the NCACT

The National Coalition Against Contraband Tobacco (NCACT) is a Canadian advocacy group formed in 2008 with the participation of businesses, organizations and individuals concerned about the growing danger of contraband tobacco. The NCACT's eighteen members share the goals of working together to educate people and urge government to take quick action to stop this growing threat.

The NCACT works to raise awareness amongst all levels of government and the public about contraband tobacco, as well as to encourage meaningful action on this important problem. More information about the coalition can be found on our website, www.stopcontrabandtobacco.ca.

The members of the NCACT are: Association des détaillants en alimentation du Québec (ADA), Association des marchands dépanneurs et épiciers du Québec (AMDEQ), Canadian Chamber of Commerce, Canadian Convenience Stores Association (CCSA), Canadian Manufacturers and Exporters, Canadian Taxpayers Federation, Canadian Tobacco Manufacturers Council, Conseil du patronat du Québec (CPQ), Customs and Immigration Union, Échec au crime Québec, Fédération des chambres de commerce du Québec (FCCQ), Frontier Duty Free Association (FDFA), National Capital Area Crimes Stoppers, National Convenience Stores Distributors Association (NACDA), Ontario Chamber of Commerce, Retail Council of Canada, Toronto Crime Stoppers and United Korean Commerce and Industry Association (UKCIA).

Why Contraband Tobacco

Contraband tobacco is a major problem in Canada. About 1 in 3 cigarettes purchased in Ontario are illegal, Quebec has identified a contraband incidence of about 15%, and police are seizing more and more illicit tobacco products heading into Atlantic Canada and the Prairies.

Contraband tobacco is a boon for organized crime, with the Royal Canadian Mounted Police (RCMP) identifying about 175 criminal gangs involved in the trade; they use the proceeds to fund their other illegal activities, including guns, drugs and human smuggling.

The social complications of contraband tobacco are reason enough to take action, but the trade has a meaningful impact on government revenues as well. Obviously, given the nature of underground economies, it is difficult to measure the exact tax loss from the illegal cigarette trade. However, a number of provincial governments and third parties have identified hundreds of millions of dollars in increased revenues from action against contraband tobacco.

In Ontario, Don Drummond's 2012 report on the future of Ontario's finances highlighted how actions such as those suggested below could increase provincial revenues by as much as \$225 million a year¹. In Quebec, estimates of tax loss were \$225 million². In New Brunswick, the fall fiscal update announced that every percentage reduction in contraband tobacco increases the province's revenues by \$1 million. Additionally, the Canadian Taxpayers Federation has estimated that tax loss for the Federal and Provincial governments in Ontario alone is as much as \$1.1 billion a year³.

If provinces are losing money to illegal cigarettes, so too is the Federal Government. Effective action against contraband tobacco hurts organized crime, increases the effectiveness of tobacco control regulations, especially those limiting youth access, and increases revenues for the Federal Government and provincial partners. These are many reasons to act.

Anti-Contraband Tobacco Budget Actions

Federal and provincial governments have introduced a number of anti-contraband tobacco measures in recent years. This include the *Tackling Contraband Tobacco Act*, which created criminal penalties for smuggling and new anti-contraband tobacco enforcement units in New Brunswick and Ontario.

However, Canada's contraband tobacco problem is an entrenched issue and these measures will not be sufficient on their own to address contraband tobacco. Moreover, the NCACT is concerned that upcoming changes to tobacco packaging regulations will facilitate an increase in contraband tobacco. So-called "plain packaging" requirements will make it easier for contraband smugglers to create illegal product, and will make it much easier for illegal manufacturers to create counterfeit cigarettes, up to now a limited market.

The NCACT has identified six straightforward areas that government can focus on to enhance its efforts on this illegal trade. They are no- or low-cost, recommended by a diverse variety of stakeholder groups, and supported by the public.

Possible anti-contraband tobacco platform items:

1) Expand RCMP anti-contraband enforcement

Anti-contraband tobacco enforcement works. There's no clearer example of this than in Quebec, which has reduced its contraband incidence by half. This was achieved through increasing powers to local police, through Bill 59, and by providing the resources they

¹ <http://www.fin.gov.on.ca/en/reformcommission/chapters/ch18.html#ch18-a>

² <http://www.budget.finances.gouv.qc.ca/Budget/2012-2013/en/documents/budgetplan.pdf>, PDF page 331

³ <https://www.taxpayer.com/media/How%20Much%20is%20Contraband%20Tobacco%20Costing%20Taxpayers%20in%20Ontario%20-%20December%202012.pdf>

need to conduct investigations, through the *ACCES Tabac* program. With these measures, Quebec has been able to decrease its incidence of illegal cigarettes by half.

RCMP anti-contraband enforcement teams, including those in Cornwall, ON and Valleyfield, QC also continue to show their value in stopping illegal cigarettes. The Cornwall Regional Task Force can serve as an effective model for such an RCMP taskforce. Quebec has demonstrated that investing in enforcement can pay clear dividends for recouping lost tax revenues from the underground economy, while also providing the social benefits associated with reducing organized crime. Recently, Ontario and New Brunswick have also introduced anti-contraband enforcement units. Bolstering and expanding federal enforcement efforts will pay similar dividends.

As just one example of the effectiveness of contraband tobacco enforcement, earlier this year law enforcement officials in Canada executed *Projet Mygale*, the largest contraband tobacco bust in Canadian history. In an operation crossing continents, 700 police officers seized more than 52,000 kg of tobacco, 5 million in cash, 836 kg of cocaine, 21 kg of methamphetamines and dismantled a supply route that illegally imported over 2200 tons of tobacco into Canada in a just over a year. Over the life of the investigation, this criminal network imported more than two million kilograms of illegal tobacco, worth \$530 million in lost taxes and enough to make billions of cigarettes.

2) Licence non-tobacco manufacturing materials, particularly filters and filter components

The RCMP has identified 50 illegal cigarette factories in Canada, each of which is able to produce as many as 10,000 cigarettes a minute. These factories are operated by organized crime groups, outside of any government regulation or taxation, and are used as a cash cow to fund their other illegal activities.

The Federal government, with Bill C-10, has increased powers for police to investigate and charge those smuggling cigarettes. It's equally important that similar efforts be made to reduce the supply of contraband cigarettes to be smuggled. This new law should be enforced immediately so that those charged can face the stiff new penalties. By licensing non-tobacco cigarette manufacturing materials the government can make it more difficult to easily produce the volumes of illegal cigarettes that make their way into Canadian communities.

Cigarette filters are the best place to start on this front. They are essential to the manufacturing process and not readily replaced. This would include ready-made filters, as well as acetate tow, the substance used in cigarette filters. Acetate tow is produced by only a handful of manufacturers globally, in contrast with actual loose leaf tobacco which can be sourced from a variety of locations and smuggled into Canada.

There is broad support for increased licensing of acetate tow from a variety of stakeholders, including health groups such as the Canadian Cancer Society, the Ontario

Medical Association and the Heart and Stroke Foundation. There would be negligible cost to government to implement such a system.

3) Audit the Federal Tobacco Tax Stamp System

Presently, federal tobacco excise stamps appear on products that are clearly contraband. These stamps were designed with the goal to more easily detect and respond to counterfeit and illicit tobacco products. However, by appearing on cigarettes that do not meet the labelling, packaging and information requirements in the Tobacco Act they actively undermine awareness and clarity among consumers⁴.

The fact that federal stamps are appearing on illegal products that do not meet Health Canada standards suggests that the current system is flawed. The NCACT recommends that the government audit the federal stamps system in order to ensure there is clarity on legal vs. illegal products. This will provide greater awareness to the consumer in regards to providing reliable information on whether tobacco products are meeting all federal guidelines.

4) Increase intergovernmental cooperation on efforts to combat contraband tobacco by leading a National Anti-Contraband Taskforce.

Contraband tobacco is a problem that crosses jurisdictional and departmental boundaries. Effective actions to address this problem will be built on collaboration between the federal and provincial governments, state and U.S. governments, private sector and First Nations leaders.

Learning from provinces that have had success in addressing the contraband problem is critical. As an example, Quebec has significantly reduced the volume of illegal tobacco in the province through effective coordination and increased enforcement efforts, which could serve as a model for other affected areas of Canada. Ontario, for its part, is pursuing revenue-sharing pilot projects with two First Nations territories. We are encouraged by the initiatives undertaken in both jurisdictions.

We believe that the Federal Government should play a leadership role to play in this collaboration. This should include appointing and leading a task force of interested parties, including those listed above, to share best practices and to explore alternative solutions, including revenue-sharing.

5) Implement a public awareness campaign regarding the risks of contraband tobacco

It is our experience that many Canadians are unaware of the dangers that illegal cigarettes offer and, in many cases, what actually constitutes contraband tobacco. As an example, the NCACT has observed that many consumers seem to be confused by the legality of tobacco products where some, but not all taxes have been paid. Similarly,

⁴See, for example: <http://www.torontosun.com/2016/01/16/the-sleeping-dog-of-contraband-cigarettes>

there is a growing trend for wholly untaxed tobacco products to look like legal, regulated product.

Given that there is an increase in offences for transport and possession of untaxed tobacco products, and that many Canadians would not intentionally break laws, there is a role for government to play in educating the public about how to correctly identify legitimate products, as well as the risks associated with using illegal ones. While this may come with some small cost, it should be offset by corresponding reductions in tax diversion to the criminal market.

6) Keep the Cornwall border crossing in Cornwall

A substantial portion of illegal cigarette manufacturing takes place near Cornwall, Ontario in territories that straddle the Quebec, Ontario, and American borders. There are more than a dozen illegal cigarette factories operating in the territory, making the area a major source of illegal cigarettes in Canada.

At present, the border crossing is located in Cornwall, Ontario, on the Ontario side of Cornwall Island. This crossing's current location was established "temporarily" in 2009, but produced a near-immediate and demonstrable improvement in stopping contraband tobacco smuggling at this crossing.

The government has proposed to move this crossing to Massena, NY as part of a larger effort to consolidate crossings. This move would be the worst possible outcome for contraband tobacco control in the area, removing any border control or inspection stations between the illegal production factories and the rest of Canada.

Consolidation of border crossings, as the Beyond the Border Action Plan highlights, makes sense at other crossings, especially those that carry a much larger portion of Canada-US cross border trade. Cornwall, however, is an exception to this, with a unique set of local circumstances that merit a different response.

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