

Cancer Council Victoria critique of KPMG LLP report on Illicit Tobacco in Australia, 2017

Prepared June 2018

On the 1st May 2018, KPMG LLP released its fifth full-year report estimating the extent of use of illicit tobacco in Australia.¹ The methodology used in this report is essentially the same as that used in previous reports. Health groups have raised major concerns about this methodology as outlined in previous critiques [here](#).

Once again in this 2018 report, KPMG LLP's estimate of the extent of use of chop chop tobacco is substantially higher than the picture painted by Australia's National Drug Strategy Household Survey.² The survey conducted by Roy Morgan Research from which tobacco companies have provided data to KPMG for use in its estimates¹ finds that 20% of tobacco smokers are using chop chop tobacco. This compares to findings of the Government's National Drug Strategy Household Survey which reports that 3.8% of smokers currently use it (up from 3.6% in 2013).

The NDSHS finds that only 1.1% of that 3.8% of smokers who use chop chop use it "half the time or more" (up from 0.8%). Most smokers who use it use it only infrequently. The KPMG LLP report however, assumes that all 20% of tobacco smokers use an amount of tobacco (2,300 grams per annum, p 52) that is close to the *total* amount of tobacco a typical smoker would consume in a year (14 cigarettes per day@0.5g per cigarette*365 days = 2555 grams per annum)—so, virtually all the time, with barely any occasional use.

It is possible that KPMG LLP consultants are applying the estimates of the frequency of purchase and amount purchased by REGULAR chop chop users to ANYONE who has used in the last year (regular and occasional alike). Or perhaps the overestimate results from the simplistic nature of the calculation. By simply multiplying the (over)estimated number of users with the average amount used, (rather than multiplying each respondent's amount purchased with each person's frequency of use and then averaging the result) they fail to take into account that amount purchased is not related to frequency of purchase in a linear way. The frequent purchasers may in fact purchase much higher amounts than the many purchasers who only buy a small amount occasionally. Whatever the reason, the estimate of the extent of use of illicit tobacco is clearly not credible. Does anyone seriously believe that 1 in 5 smokers smoke unprocessed tobacco from a plastic bag, *every day*?

¹ The participants in the illicit tobacco survey are not randomly selected but rather are drawn from a panel of people who have taken part in the company's well regarded ongoing monthly household survey, and then go on and agree to participate on a paid basis in additional research projects, and then this project in particular. No information is provided about the numbers of respondents in the 2017 illicit tobacco survey who have participated in the illicit tobacco survey in previous years. In fact no information is provided at all about the respondents. It could be that those who agree to participate in the study each year are more likely to be unemployed, or more likely to smoke RYO tobacco, more likely to have participated in previous years or more likely to possess other characteristics that predispose them to be a regular chop chop user.

The estimate of the amount of chop chop used makes up almost 50% of the total estimate of the market in this (2017) report, and an even higher proportion in previous reports. The obvious overestimation of the chop chop component undermines the credibility of the entire series of KPMG LLP reports.

The other element of the estimated total size of the illicit market is the estimated number of contraband cigarette packs. KPMG's estimate of use of contraband packs has gone up, especially so in Melbourne. This could be correct, but the quantification of the size of the contraband market is still likely to be an exaggeration for reasons described in full in previous critiques. In brief, people most likely to be buying packs originating from overseas—being travellers, recent migrants and international students or special visa workers—are much less likely to be motorists and much more likely to be walking and using public transport. The packs they use are therefore much more likely to enter the litter stream in public places than are packs used by smokers who do not travel frequently overseas.

There is still no evidence of any counterfeiting of brands sold in plain packs by major three companies, though there do now seem to be a couple of plainly packaged brands produced specially for the illicit market. (Customs duty may have been paid on these, but impossible to tell at the retail level without tax stamps with covert authentication marks.)

It is interesting that the **report states that the legitimate market declined by 6.9% between 2016 and 2017 (p10). (Loose tobacco up by 5.8% but manufactured cigarettes down by 9.2%, resulting in total decline of 6.9%).**

The report itself estimates that the total volume of illicit tobacco consumed **declined by 1%** (p 6).

This results in a total (legal and illegal) decline of 6.1%. ... very much in line with what you'd expect from price rises resulting from the 12.5% increase in excise duty. So... no evidence of effectiveness of tax increases declining.

Thankfully the Australian Tax Office has recently released an independent assessment of the extent of use of illicit tobacco in Australia. This puts the problem at \$731m in lost revenue in 2015-16 (\$594m once you add back in the recovered tobacco from raids). This compares to the \$1.61b claimed by the 2016 KPMG report. Not a lot of detail is provided about the calculations, but the ATO estimates do seem to be based on much more solid intelligence and information and are much more plausible.

Details of the tobacco tax gap are available on the ATO website <https://www.ato.gov.au/About-ATO/Research-and-statistics/In-detail/Tax-gap/tobacco-tax-gap/>

Further information on Australia Tax Gaps can be found [here](#).

References

1. KPMG LLP. Illicit tobacco in Australia: 2017 full-year report. London 2018. Available from: <https://home.kpmg.com/uk/en/home/insights/2018/05/illicit-tobacco-in-australia-2017.html>.

2. Australian Institute of Health and Welfare. National Drug Strategy Household Survey 2016 Key findings. Online data and reliability tables Canberra: AIHW, 2017. Available from: <http://www.aihw.gov.au/alcohol-and-other-drugs/data-sources/ndshs-2016/data/>.