

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

Written Submission for the Pre-Budget Consultations in Advance of the Upcoming Federal Budget

February 2022

Recommendations

Recommendation 1

That the Government of Canada partner with the Government of Ontario in taking action against contraband tobacco in the province, where the highest rates exist and where the federal government's tobacco control measures are the most undermined.

Recommendation 2

That the Government of Canada increase funding to the Royal Canadian Mounted Police for contraband tobacco enforcement.

Recommendation 3

That the Government of Canada resume a prudent approach towards tobacco taxation until contraband tobacco is addressed across Canada.

Introduction

Smokers and non-smokers alike have been widely impacted by the economic shutdown caused by the COVID-19 pandemic. While many Canadians are getting back to work, millions are still unemployed and millions more have lost income and savings. Overall, the buying power of millions of Canadians has been reduced due to the COVID-19 pandemic.

Concerning contraband tobacco in Canada, this situation raises both opportunities and large risks for provincial and federal governments. Prior to the COVID-19 pandemic, one in three cigarettes purchased in Ontario were illegal, accounting for a combined federal-provincial excise tax loss of over \$1 billion annually. Nationally, contraband tobacco accounts for over \$2 billion in lost taxes to both levels of government. During the pandemic, an Ernst & Young report commissioned by the Convenience Industry Council of Canada found that sales of legal tobacco increased by nearly 24% due to lockdowns.¹ The Royal Canadian Mounted Police (RCMP) estimate there to be approximately 175 organized crime groups involved in the illicit tobacco trade, who make millions of dollars almost daily from contraband tobacco. They use these proceeds of crime to fund other illicit activities, such as the sale and distribution of illegal cannabis, cocaine, fentanyl, guns and human trafficking.

Evidence shows that contraband tobacco is sold and distributed in every Canadian province. As a result of the growing prevalence of contraband tobacco, individual provinces such as Manitoba, Quebec and New Brunswick have taken specific actions to combat the illicit tobacco trade as a means to combat criminal activity that includes human trafficking, as well as the distribution and sale of illicit drugs and firearms. Further, provincial governments have seen first-hand how the illicit tobacco trade has cost them billions of dollars in annual revenue, a financial gap that must be filled as we look towards Canada's post-COVID economic recovery.

Contraband tobacco is one of the most lucrative illicit trades. For example, a 400% profit can be made off of illegal cigarettes, compared to a 50% profit for cocaine and 100% profit for cannabis at the street level. It has been proven that these large sums of profit for organized crime groups also fuels money laundering schemes in Ontario and beyond. Due to this, provinces have found that enforcing contraband tobacco is one of the few public safety investments that will increase overall government revenues.

While other provinces have made the investments in combatting contraband tobacco, Ontario continues to lag behind. The situation has worsened recently due to the heavy tobacco tax increases included in the federal government's Budget 2021. Without Ontario taking action against contraband tobacco, and with the Government of Canada's tobacco taxation policies helping drive smokers to the illicit tobacco market, criminal gangs will continue to profit to the tune of millions of dollars each day. The National Coalition Against Contraband Tobacco (NCACT) contends that the following recommendations, if implemented, would help to more effectively combat organized crime groups and protect Canadians from an unregulated, illegal, product while preventing the loss of millions of dollars in revenue to public treasuries.

¹ https://convenienceindustry.ca/wp-content/uploads/2020/12/Impact-of-COVID-19-on-Contraband-Tobacco-and-Provincial-Tax-revenues-in-Canada_EN-Final.pdf

Stopping the Flow of Contraband Tobacco

While manufacturing of illegal cigarettes takes place in both Ontario and Quebec, it is largely centred in Ontario where illicit factories can churn out 10,000 cigarettes per minute through some of the most sophisticated equipment available. The contraband tobacco market has become efficient and organized due to a lack of robust, concerted, action taken against it by both federal and some provincial governments. However, Quebec continues to lead the way in contraband tobacco enforcement and provides a model that other provinces should consider replicating.

Prior to 2009, Quebec had the same contraband tobacco issue as Ontario, where one in three cigarettes sold were illegal. In 2009, in order to more effectively counter tobacco smuggling, the Government of Quebec passed *Bill 59: An Act to amend the Tobacco Tax Act* and other legislative provisions². As a result of Bill 59, Quebec successfully reduced its rate of contraband tobacco from approximately 33% to 12% within two years³ allowing the government to realize millions of dollars of otherwise lost revenue within a two-year timespan.

Bill 59, the provisions of which remain in force today, took three specific actions:

1. It allowed all police officers in Quebec to conduct full contraband tobacco investigations;
2. It created *Accès Tabac*, a program to fund ongoing contraband tobacco investigations; and,
3. It created a 54-member Contraband Tobacco Enforcement Team at the *Sûreté du Québec*.

Quebec's 2020 budget documented that the government spent \$14.4 million on its contraband tobacco program and yielded a return of \$206 million⁴; a return of over \$14 for every one dollar invested by the Government of Quebec. The Quebec model is a proven path forward for Ontario, and other provinces, wishing to take effective action against contraband tobacco.

The COVID-19 pandemic has temporarily transformed the contraband tobacco market. In Ontario, as a result of the lockdown of reservations, primarily in the southwestern part of the province, contraband tobacco rates have decreased due to consumers being unable to access the illicit product. However, organized crime groups continue to operate their illicit trade routes, distributing millions of illegal cigarettes across Ontario and Canada.

The opportunity for the governments of Canada and Ontario to take action has been highlighted by the current situation. Indeed, the federal Department of Finance and the Ontario Ministry of Finance should use the past 17 months as a case study for what revenue from excise taxes might look like if concerted action was taken. The circumstances around COVID-19 related lockdowns have inadvertently allowed for Canadian tobacco control measures to take effect, which are not currently in place for contraband tobacco.

The risk for both levels of government is during the post-COVID recovery phase. As millions of Canadians find themselves unemployed and millions more see a reduction in their overall buying power, there is a large risk that the contraband tobacco market will see an upsurge once the aforementioned reservations end their lockdowns. Smokers, who may be unwilling to pay a higher cost for legal cigarettes, are likely

² <http://www.assnat.qc.ca/en/travaux-parlementaires/projets-loi/projet-loi-59-39-1.html>

³ http://www.budget.finances.gouv.qc.ca/budget/2019-2020/en/documents/AdditionalInfo_1920.pdf

⁴ http://www.budget.finances.gouv.qc.ca/budget/2020-2021/en/documents/Budget2021_AdditionalInfo.pdf

to begin smoking illegal cigarettes. This will further undermine tobacco control measures and further increase the loss of excise taxes at a time when federal, provincial and territorial governments are in need of revenue.

Through Canada's Tobacco Strategy, the Government of Canada has set itself an ambitious goal of driving down smoking rates to less than 5% by 2035. About 15%⁵ of the population continue to smoke in Canada, with 33% in Ontario smoking illegal cigarettes. While we commend the government's plan, the goals set out in the strategy cannot be achieved without acting against contraband tobacco. The illicit market ignores all tobacco control measures including selling to minors, plain packaging regulations and health warnings. Without targeted, aggressive, action against the contraband tobacco market the federal government will be hard pressed to get close to 5% by 2035.

While Quebec has seen widespread success in combatting contraband tobacco, Ontario continues to be the epicentre of the illegal trade. The issue continues to be inter-provincial and one that the national government must address. As a starting point, the Government of Canada must partner with the Government of Ontario in combatting the illicit market, enforcing tobacco control measures and taking away millions of dollars from organized criminals. By working together, we believe both governments can make discernible, lasting, progress in addressing Ontario's role as the epicentre of Canada's illicit tobacco trade.

Recommendation

That the Government of Canada partner with the Government of Ontario in taking action against contraband tobacco in the province, where the highest rates exist and where the federal government's tobacco control measures are the most undermined.

Supporting the RCMP

The Royal Canadian Mounted Police (RCMP) acts as the provincial police force for every province with the exception of Ontario, Quebec and Newfoundland and Labrador. While the individual provincial police services are jointly funded by participating provincial governments and the federal government, provincial RCMP services continue to be limited in their enforcement resources at a time when the illegal cigarette trade continues to grow; this growth must be matched with an increase to the RCMP budget in order to address this threat to national security.

Furthermore, the Government of Canada must make clear to the RCMP that contraband tobacco is a priority on the same scale as the trafficking of narcotics and opioids. That said, the RCMP in New Brunswick are a good example of a police service that works closely with the New Brunswick Department of Justice and Public Safety in combatting contraband tobacco and ensuring that it remains a top priority. Through targeted funding and collaboration between the RCMP and provincial departments of public safety, the Government of Canada can better support provinces in combatting illegal cigarettes.

Recommendation

That the Government of Canada increase funding to the RCMP for contraband tobacco enforcement.

⁵ <https://uwaterloo.ca/tobacco-use-canada/adult-tobacco-use/smoking-canada/current-smoking-prevalence>

A Prudent Approach to Tobacco Taxation

In Budget 2021, without any consultation with the provinces and police services, the Government of Canada increased the tobacco excise duty by \$4 per carton of 200 cigarettes. This is in contrast to the majority of provincial governments who have taken a prudent approach to tobacco taxation in response to increased revenue due to the COVID-19 pandemic.

A report by Ernst & Young, commissioned by the Convenience Industry Council of Canada, found that COVID-19 lockdowns had dramatically impacted the illicit trade of illegal cigarettes, increasing federal and provincial tobacco tax revenues by over \$50 million in June 2020. The report also found that contraband tobacco is about 24% of Canada's total tobacco market.⁶

Furthermore, the Parliamentary Budget Officer in a Legislative Costing Note found that the tobacco tax increase in Budget 2021 would not increase government revenue and indicated that past federal excise tax increases on tobacco have inadvertently helped the contraband tobacco market to thrive. Additional evidence has also shown that steep tax increases at the federal or provincial level have driven smokers to the black market due to illegal cigarettes being accessible and around a third of the cost of the legal product. To ensure that fewer smokers are encouraged to begin purchasing cigarettes from organized crime groups, we recommend that a prudent approach to tobacco taxation be resumed at the federal level.

Recommendation

That the Government of Canada resume a prudent approach towards tobacco taxation until contraband tobacco is addressed across Canada.

About

The National Coalition Against Contraband Tobacco is a Canadian advocacy group formed with the participation of businesses, law and order organizations and individuals concerned about the growing danger of contraband cigarettes. Our members share the goals of working together to educate people and urge government to take quick action to stop this growing threat. To learn more, please visit www.stopcontrabandtobacco.ca.

⁶ https://convenienceindustry.ca/wp-content/uploads/2020/12/Impact-of-COVID-19-on-Contraband-Tobacco-and-Provincial-Tax-revenues-in-Canada_EN-Final.pdf