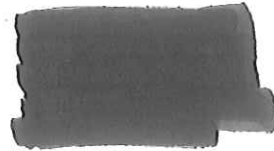




Robin Cartwright
Partner

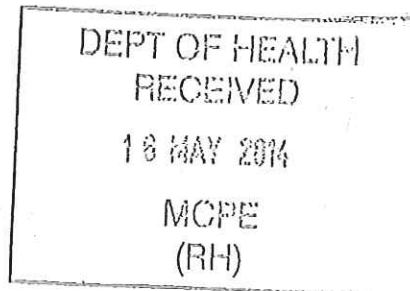
KPMG LLP
Transaction Services
15 Canada Square
Canary Wharf
London E14 5GL
United Kingdom



Private & confidential
Jane Ellison MP
Parliamentary Under Secretary for Public
Health
Department of Health
Richmond House
Whitehall
LONDON
SW1A 2NS

Our ref rc/af

Contact Robin Cartwright



2 May 2014

Dear Ms Ellison MP

Subject: KPMG Response to Criticisms of its 'Illicit Tobacco in Australia Report' in the Chantler Review

I thought it may be helpful to clarify some of the public commentary and some criticisms by Sir Cyril Chantler's independent review "Standardised Packaging of Tobacco" of KPMG's recent report on "Illicit Tobacco in Australia".

Public commentary and KPMG's position

KPMG has no views on proposals for plain paper packaging. However, the report we released recently "Illicit tobacco in Australia – 2013 Half Year Report" has been somewhat misrepresented by others, without our consent, to suggest it supports the contention that plain paper packaging could lead of itself to an increase in tobacco smuggling and duty avoidance. KPMG's report is an independent piece of work, which gives a reliable insight into the level of illegal tobacco consumption. It is a factually-based survey of illicit tobacco consumption and does not, indeed cannot, comment on the potential links between illicit tobacco and government policy, price, excise or enforcement activity. It should be viewed as a piece of standalone data analysis.

Context behind Chantler's review and our participation

In 2013 KPMG took over this periodic report on Australia's illicit tobacco trade from Deloitte, who had published reports up to 2012. We applied our own methodology, adapted from our seven-year Project Star looking at illicit flows in EU countries, undertaken for both Philip Morris and the European Commission's OLAF.

Two representatives from the Chantler Review contacted us to discuss the Australian report's findings. We met them in February 2014, and had a series of follow up discussions, providing

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additional data and clarification at their request. But at no point did these representatives seek to obtain our comments on their alternative estimates, or on the draft sections of the Report itself which mentions KPMG's work, which we would have expected.

The Specific Criticisms, by Chantler, of KPMG's report and our response

The Chantler review chose to dismiss our report's findings on the basis of two pieces of evidence, one of which actually supports our report and the other of which is unusable given timing differences. We set out below the rationale for this in the two notes, which refer to the two specific claims in the Chantler report.

Paragraph 5.6 of Chantler's report is extracted below.:

"Tobacco manufacturers cite the industry funded KPMG report on illicit tobacco in Australia, 72 which purports to show that there has been a large increase in illicit trade since the introduction of plain packaging. I have considered both this report and a critique.⁷³ My team have also met with KPMG in order to understand their methods. 74 I note that Australian Government departments, both Health and Customs, appear to be strongly of the view that KPMG's methodology is flawed. These Departments point to official Customs data, 75 which shows no significant effect on illicit tobacco following the introduction of plain packaging (*Note 1*), backed by analysis undertaken by the Cancer Council Victoria (based on data from the National Drug Strategy Household Survey) that suggests that illicit tobacco in Australia is only 10-20% of the level proposed by KPMG (*Note 2*).⁷⁶ In a situation where estimates differ by such magnitudes, I do not have confidence in KPMG's assessment of the size of – or changes in – the illicit market in Australia."

Note 1. This appears incorrect. However you analyse the Australian Customs & Border Protection Service (AC&BPS) data for the period in question, 2012-13 shows a rise in unbranded loose tobacco, as did our report, and a much greater rise in manufactured cigarettes, as did our report.

Annual Seizures Data			
	2012	2013	2012-2013
Tobacco including molasses (tonnes)	136.2	204.1	50%
Cigarettes (tonnes)	89.2	158.6	78%
Total (tonnes)	225.4	362.7	61%

Source: Australian Customs & Border Protection (AC&BP)

Note 2. This data appears incomparable with our own. It is taken from a consumer survey conducted in 2010 and therefore not comparable with our 2013 data. Moreover the survey, the National Drug Strategy Household Survey (NHDHS) was not designed to assess the quantum

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of illicit trade. Cancer Council Victoria (CCV) has then extrapolated from this household survey by using assumptions on average daily use (as the survey does not ask about amounts consumed). CCV then 'gross up' the number for manufactured cigarettes (which again the survey does not cover) from Customs' seizure data from 2010/11 (when manufactured cigarettes were still a small part of the overall problem – now they are over half of the problem, by Customs' own admission). This '10-20%' range would indicate that customs are seizing around 79% to 157% of all illicit products, which would be an unprecedented seizure rate. The World Customs Organisation suggests seizures are around 10-15% of the illicit market. Our report indicates a seizure rate of around 13%.

In short, this very low level of illicit (c.2%), in one of the highest priced markets in the world, is not credible in our view.

We appreciate that the DH will want to draw from a range of available evidence of which our report is a part but we are absolutely of the view that our methodology is robust, widely used and independently validated, and that Chantler has chosen too lightly to dismiss the findings without a thorough explanation. The professional integrity and independence of our work is very important to KPMG and we feel that this should be properly recognised. Please do not hesitate to contact me if you have any further queries.

Yours sincerely



Robin Cartwright
Partner, KPMG LLP

cc The Right Honourable The Earl Howe, House of Lords, SW1A 0PW



Department
of Health

Tobacco Programme
6th Floor
Wellington House
133-155 Waterloo Road
London
SE1 8UG

www.dh.gov.uk

Mr Robin Cartwright
Partner
KPMG LLP
Transaction Services
15 Canada Square
London
E14 5GL

27 June 2014

Dear Mr Cartwright,

I am responding to your letter to the Public Health Minister Jane Ellison dated 2 May 2014 regarding your company's *Illicit Tobacco in Australia Report*. The Minister has asked me to thank you for writing and to reply on her behalf.

It is useful to understand the position of your company with respect to standardised packaging, and that the report does not comment on links between illicit tobacco and government policy, price, excise or enforcement activity. We are aware of the "public commentary and some criticisms" of the report that you mention in your letter and taken note of the "important notice" that is provided to suggest how the report be used. You say that the KPMG report has been "somewhat misrepresented" by others, without your consent, to suggest it supports the contention that plain packaging could lead of itself to an increase in tobacco smuggling and duty avoidance.

Health ministers have been clear that they want to be cautious about data on illicit tobacco, and to rely on official statistics in this area wherever possible. In the United Kingdom, for example, Her Majesty's Revenue and Customs annually publish data on the size of the illicit tobacco market.

Regarding the manner in which the KPMG study was undertaken, I note that you applied your own methodology, adapted from your seven-year Project Star looking at illicit tobacco flows in EU countries. To maximise transparency and to demonstrate the independence of your work, I suggest that it would be worthwhile for KPMG to put the full methodology that was used for both this Australian report and Project Star into the public domain.

Regarding standardised packaging of tobacco products, you might also be interested to know that on 26 June 2014 the Government published the *Consultation on the Introduction of regulations for standardised packaging of tobacco products* on the web at:

<https://www.gov.uk/government/consultations/standardised-packaging-of-tobacco-products-draft-regulations>

The Government has not made a final decision on whether to introduce standardised packaging. Before reaching a decision on whether to introduce standardised packaging of tobacco products, the Government is holding this final, short consultation. This consultation will run for six weeks until 7 August 2014. So that the decision on whether to introduce standardised packaging is properly and fully informed, the consultation includes a set of draft regulations so that it is clear how such a policy would work in practice. The draft regulations set out proposed requirements for the packaging of cigarettes and hand-rolling tobacco, and requirements for the appearance of individual cigarettes, should standardised packaging be introduced.

In the consultation the Government asks, in particular, for views on anything new since the last full public consultation on standardised packaging that was run in 2012 that is relevant to the development of this policy, including evidence relating to the wider implications of introducing standardised packaging. I recognise that you have said in your letter that KPMG has no views on proposals for standardised packaging. However, if after looking at the consultation document you wish to provide views or relevant evidence, I would encourage you to do so.

[REDACTED]

[REDACTED]