THE TOBACCO INSTITUTE OF SOUTHERN AFRICA

SA becomes first country in the world to allow an illegal cigarette brand to become the top seller

Johannesburg, November 27, 2018 – The trade in illegal cigarettes has increased dramatically, despite promises of a crackdown from the South African Revenue Service (SARS), according to the latest Tobacco Market Study from research house Ipsos. Cigarettes selling for less than the tax of R17.85 per pack owed to SARS have grown market share by over 25%, from 33% to 42% in the informal market, in just three months. According to a 2015 judgment, cigarettes that sell for below the minimum tax can be deemed as illicit.

In a remarkable show of defiance, manufacturers of cigarettes selling below the minimum tax have expanded their distribution at the very same time as SARS has been promising to crack down. Gold Leaf Tobacco's RG brand is now the top selling brand in South Africa overall, overtaking all legal brands. It sells for an average price of just R10 and is, therefore, clearly evading the R17.85 owed to SARS on each pack.

Gold Leaf Tobacco Corporation (GLTC) now represents 73% of the market for illegal cigarettes. It is on track to become the biggest tobacco company by sales volume in the country, especially if there is another tax increase on legal cigarettes in February 2019.

GLTC's biggest challenger is Best Tobacco Company whose brand, Caesar, also retails for R10 on average and is now the second fastest growing cigarette brand in the country, after RG. Its growth has been driven by its expansion into the Eastern Cape. Ipsos's research indicates that 95% of Best Tobacco's sales are illicit.

Their prices are 73% cheaper than the reference price in the legal market used by Treasury to determine excise duties, and 44% cheaper than minimum taxes owed on each pack.

Earlier this month, the Nugent Commission of Inquiry found that "those who trade illicitly in commodities like tobacco operate with little constraint". The Ipsos research counts the cost of this failure of government.

The latest Ipsos retail audit – conducted in September and October – is the second wave of a tracking study that was first run in May and June this year. It audited a representative sample of 2,058 retail outlets twice in each wave, using a methodology that has been peer reviewed by local and international research experts and academics. The research was commissioned by the Tobacco Institute of Southern Africa (TISA).

Prof. Nicola Theron, Managing Director of Econex, attended a briefing by Ipsos on the results of the second read and said, "This is valuable research and should urgently inform government policy and action to clamp down on illegal cigarettes, to maximise government revenue via tax collection. The methodology appears sound and therefore the findings seem to be robust and conservative."

In the three months since the first wave, tobacco products below the minimum tax due have soared from 33.1% in June to 41.8% in the informal retail sector. This means that SARS is now losing at least R8 billion annually; up from R7 billion reported in the previous wave of the Ipsos study.

It is six weeks since Judge Robert Nugent recommended the appointment of a permanent SARS Commissioner as an essential first step in rebuilding SARS's ability to collect taxes from those who don't pay willingly. The slow pace of reform, together with February's tax increases, have awarded another year of unimpeded tax fraud to illegal cigarette companies registered by SARS.

"Until government is able to collect taxes from those who evade paying, it should think extremely carefully about increasing taxes again on the legal market," said TISA Chairman François van der Merwe.

"In these circumstances, another tax increase would be a betrayal of the 12,000 workers whose jobs depend on the legal tobacco sector.

"Worse still, it would send a message to South Africa that the government wants to discourage the consumption of tax-paid cigarettes, but is relatively relaxed about the consumption of illegal cigarettes.

"Increasing taxes is easy, but not a solution." said Van der Merwe. "Rather, collecting taxes from those choosing not to pay is the best place to start."

ENDS

NOTES TO EDITORS

1. The Ipsos Tobacco Market Study investigated brands retailing below the minimum tax due of R17.85. It is possible that some brands selling at or above this level have also not paid taxes.

2. That these products are illegal has been established in a 2015 judgment in the Eastern Cape High Court. In that case, relating to sales of a GLTC brand for R8 per pack, the judge found that "The logical inference to be drawn is that no excise duty was paid in respect of the cigarettes in question."

3. It is sometimes claimed that cigarette sales below the taxes due are counterfeit. This is simply impossible. Taking RG as an example, 89% of its sales are below the minimum tax owed. It is not credible that almost all sales in a particular brand are from counterfeiters and not the brand owner.

4. TISA is the industry body for the legal tobacco sector in SA.

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