

A submission presented on behalf of



To the Legislative Assembly of Ontario
Standing Committee on Justice Policy

In consideration of

Bill 155: An Act to permit the Province to recover damages and health care costs incurred because of tobacco related diseases and to make a complementary amendment to the Limitations Act, 2002

May 6, 2009

SUBMISSION TO THE LEGISLATIVE ASSEMBLY OF ONTARIO

STANDING COMMITTEE ON JUSTICE POLICY

INTRODUCTION

Imperial Tobacco Canada Limited (“ITCAN”) provides the following submissions to the Standing Committee on Justice Policy regarding *Bill 155: An Act to permit the Province to recover damages and health care costs incurred because of tobacco related diseases and to make a complementary amendment to the Limitations Act, 2002* (“the Bill”). The Bill proposes to give Ontario a direct and distinct action against manufacturers of tobacco products to recover the cost of health care benefits caused or contributed to by a tobacco related wrong, and enacts special rules to be applied in such actions.

SUMMARY OF MAIN CONCLUSIONS AND RECOMMENDATIONS

ITCAN submits that the Bill should not be passed by the Legislative Assembly, for the following reasons:

1. The “Medicaid Action” proposed by the Bill is unlikely to succeed, nor will it result in a settlement like that achieved in the United States.
2. Even were the Medicaid action to succeed, Ontario would not recover substantial sums of money in the foreseeable future given the high legal fees and the lengthy timescale associated with such an action.

3. In addition, success for the province in any Medicaid action would likely have the result of bankrupting the legitimate Canadian tobacco manufacturers, which would not only deprive Ontario of any significant recovery in the action, it would also leave the Ontario tobacco market in the hands of illicit operators.
4. The manner in which the Bill “stacks the deck” in favour of the province in any Medicaid lawsuit creates a dangerous precedent for the province’s relationship with other businesses.
5. Ontario – and the tobacco manufacturers – should instead be devoting their resources to combating the illicit trade in tobacco products, given the overwhelming growth of this trade in Ontario and the threats it poses to government revenues, public health policies and to the livelihoods of Ontario’s small retailers.

IMPERIAL TOBACCO CANADA LIMITED

Established in 1908, ITCAN is Canada’s largest tobacco manufacturer. ITCAN employs over 800 individuals at its main office and regional sales offices throughout Canada, including Ontario. Currently, ITCAN, through trademarks such as du MAURIER, Player’s, Peter Jackson and Matinée, offers quality products to over five million Canadian adults who choose to smoke.

We are dedicated to acting in a responsible manner and meeting the broader community’s expectation on how a modern tobacco company conducts its business.

The input of ITCAN as the largest legitimate Canadian tobacco company is essential to achieve government health objectives, which must be pursued in an atmosphere of respect for individual rights and collective interests consistent with a democratic society. ITCAN wishes to stress that, as a legitimate tobacco company, its opinions deserve the same consideration as those of other stakeholders and hopes that the observations and suggestions made in this brief, which are respectful of the rights of smokers and non-smokers alike, will be received with the open and objective attitude that is required of a government.

THE POLICY OF THE BILL

From the *Toronto Star*, December 12, 2006

Premier Dalton McGuinty said the provincial government — which brought in one of North America's toughest anti-smoking laws last May — is concentrating on public education campaigns and quit-smoking programs instead of a lawsuit.

“The other agenda is about punishing Big Tobacco,” McGuinty said yesterday. “We have not embraced that agenda. That does not serve our purposes.”

McGuinty said the province plans to “wait and see” how things work out with British Columbia’s lawsuit against tobacco giants.

The governments of British Columbia, Saskatchewan, Manitoba, New Brunswick, Nova Scotia and Newfoundland have already passed legislation — or are in the process of doing so — enabling them to sue tobacco companies.

“There is some considerable doubt associated with a successful suit here in Canada,” McGuinty added. He said British Columbia has already spent some \$20 million on pursuing the tobacco lawsuit, “with no end in sight, (or any) reasonable prospect of returns in sight.”

Nothing has changed in the last two years to invalidate the view expressed by Premier McGuinty in 2006 on the wisdom of so-called “Medicaid Suits” against tobacco manufacturers. Medicaid

lawsuits are doomed to fail in Canada and do not advance public health policy. Medicaid lawsuits do not stop smokers from smoking; they simply enrich lawyers. Ontario taxpayers will never recover the tens of millions of dollars the province will be required to pay to pursue Medicaid litigation.

Rational tobacco policy would involve shunning such a wasteful litigious approach in favour of developing policies to fulfill government's legitimate public health responsibilities. ITCAN believes that a more co-operative, non-confrontational relationship between regulators and tobacco manufacturers is the most pragmatic way to advance public health in the area of tobacco.

Chance of Success

The provinces of British Columbia and New Brunswick are suing tobacco companies for health care costs allegedly incurred as a result of the use of tobacco. We believe these lawsuits are unfounded. The sale of tobacco products is a legal business and government in its role of regulator has had full knowledge of the risks of smoking for decades. Moreover in a very real sense, government has been the senior partner in the industry in Canada. Today governments collect approximately \$9 billion a year in taxes from the tobacco industry (18 times more than the profitability of all the tobacco companies combined), and have collected a total of \$130 billion since 1970. In addition to being a beneficiary of substantial tax revenues from tobacco, the Ontario government has also played an historical role in supporting tobacco growers in the province, most noticeably by administering the Ontario Flue-Cured Tobacco Growers' Marketing Board, whose members supply almost all of the tobacco used in Canadian tobacco products.

There is no parallel between Canadian Medicaid actions and the litigation that led to the 1998 Master Settlement Agreement in the United States, in which U.S. tobacco companies agreed to pay State governments \$250 billion over 25 years and accept new regulatory requirements. American tobacco manufacturers were able to pay for this settlement (which did not involve any admission of guilt on the part of the tobacco companies), by charging higher prices to U.S. consumers for their tobacco products. The excessive level of tobacco taxes in Canada - which has already given birth to an unprecedented illicit market in tobacco products - makes it impossible for Canadian tobacco companies to raise tobacco prices to any significant degree. In addition, Canadian tobacco manufacturers already face considerably more stringent regulations than those agreed to by U.S. companies in the Master Settlement Agreement.

Further it must be remembered that the claims of U.S. states represented only a few among a much larger number of "health care costs recovery" actions which were brought by various parties who paid health care costs to treat persons who were alleged to have suffered tobacco-related illnesses. Out of a total of nearly 200 such cases brought by insurance companies, municipalities, trade unions etc., only a handful are still pending. Virtually all of the remaining such cases were dismissed or withdrawn with the plaintiffs recovering nothing.

Finally, it should be stressed that very little financial assistance, if any, was made available to U.S. tobacco control programs as a result of the Master Settlement Agreement. The vast bulk of the settlement monies paid by U.S. tobacco companies went, first into the pockets of the very wealthy lawyers who acted for the States in the course of the litigation, and then to various diverse projects that had nothing to do with smoking and health. Most controversially, U.S. lawyers acting on behalf of the States, or in support of the States' litigation, were paid more than \$13 billion in connection with this settlement.

Cost to taxpayers

As Premier McGuinty observed, by 2006 the Government of British Columbia had already spent in excess of \$20 million in connection with its attempt to bring a Medicaid lawsuit. Considerably more than that has now no doubt been spent. This lawsuit suit is still many years from reaching a final judgment. The province of Ontario will be in for a similarly long, hard and expensive fight if it chooses to go down the same road as British Columbia. Any results of such a choice would not be seen until long after the mandate of the current Ontario government comes to an end. If, as we believe, the lawsuit is ultimately unsuccessful, the Ontario taxpayer would be left with nothing but legal bills, not only those of the province's own lawyers, but also the substantial costs that the province would be bound to pay the manufacturers for their defence legal expenses. The results of a successful lawsuit might even be worse: the bankruptcy of the legal manufacturers. This result would not only detrimentally affect the financial recovery of the government; it would, more importantly, leave the Ontario tobacco market completely in the hands of illicit manufacturers and distributors. The tobacco market in Ontario would thereafter be unregulated and unsupervised; Ontario would lose billions of dollars in tax revenue; and Ontario smokers would be supplied by criminal organizations who would utterly disregard all production safety requirements, all health regulations, all labelling and packaging requirements and all youth access retail controls, as indeed they now do, with federal and provincial governments doing very little if anything to stop them.

Attack on a legal industry

In the unlikely event that Medicaid actions in Canada were to succeed, the figures which have been advanced as potential damages by those Canadian provinces engaged in or contemplating Medicaid suits is simply more money that the Canadian tobacco manufacturers could ever afford to pay. It is not in the interest of Canadian governments or Canadian consumers to put the present tobacco manufacturers into bankruptcy. Canadian tobacco companies are closely regulated; they collect and remit significant tax revenue and they comply with applicable laws and regulations. Smokers would not stop smoking if the major companies were bankrupted. Instead governments would find themselves dealing with illicit renegade manufacturers, manufacturers who currently do not pay taxes or comply with tobacco regulations. Should the legal manufacturers go out of business, our view is that illicit manufacturers have the manufacturing capacity and a sufficiently developed supply chain to pick up any shortage and take over the entire Ontario tobacco market in a matter of days. By bankrupting the legal companies, the government would also lose significant sources of income and corporate taxes and have to deal with the loss of potentially thousands of Canadian jobs in the tobacco industry, meanwhile achieving only scant returns on any damages awarded in the Medicaid lawsuit itself.

Unfairness of Bill

While we question the wisdom of the province choosing to devote its energy and resources to a wasteful and protracted litigious process, we also object to the manner in which the Bill allows the province to unfairly use its legislative powers to “stack the deck” in its favour to its benefit as a potential plaintiff before the courts. The Bill would take away normal rights enjoyed by the defendants to any civil lawsuit in Ontario. The Supreme Court of Canada may have

accepted that a province has a constitutional right to enact such self-serving legislation, but the fact remains that the exercise of such a right remains fundamentally unfair and distasteful.

More importantly, this is just one of the ways in which the Bill sets a dangerous precedent for future legislation outside the area of tobacco control. If the legislature decides to “change the rules” to benefit the province in the civil courts in this instance, the door then lies open for the government to cause the legislature to do so again whenever the government goes to court in the capacity of a private litigant. This may in turn lead to an unwillingness on the part of the private sector to deal with the government, knowing that the legislature might at any moment decide to “make up the rules as it goes” for any lawsuit involving the government as a party.

It is also unnecessary to pass the Bill for Ontario to acquire the right to sue tobacco manufacturers in tort for health care costs allegedly caused by negligence. Such a right has already been legislated under the *Ministry of Health and Long Term Care Statute Law Amendment Act, 1999*, S.O. 1999, c.1.

Alternatively, in the event the Bill were passed it is by no means necessary for the province to actually commence litigation immediately thereafter. The government should consider again the wisdom of Premier McGuinty’s previously avowed “wait and see” approach. By observing carefully the progress of the actions in British Columbia and New Brunswick, rather than launching itself and its lawyers immediately into the fray, Ontario will be better able to assess whether Canadian Medicaid actions are able to accomplish anything beyond the waste of taxpayers’ money. In addition, if one of the provinces is indeed successful, then Ontario would be able to file a claim as with any other creditor. First to sue does not give any preferred rights.

Finally, the whole idea of Medicaid suits should be of concern to other businesses whose products are (or might become) subject to complaints about their associated health risks. Pharmaceutical companies, alcohol companies, pesticide companies, fast food restaurants: all of these have at various times had their products brought under the public health microscope in connection with possible health risks caused to their consumers. These businesses might well be prepared to respond to product liability lawsuits brought by individual consumers, or even class actions. Ironically, two of the more obvious candidates for such lawsuits, gambling and alcohol, are already owned or controlled by governments. But such businesses should now worry about their potential to be the next targets of legislation of this type. Once carried into effect in this Bill, there will be no end of potential applications for this process against other businesses in the future.

ILLICIT TRADE IN TOBACCO PRODUCTS

On numerous occasions, ITCAN has warned the Ontario government that the trade in illicit tobacco products is taking on phenomenal proportions in this province. Ontario leads the country in the extent of its illicit tobacco market. In fact Ontario's illicit tobacco market is so bad, that the rate of illicit trade in this province is higher than that of Nigeria, Zimbabwe, Brazil, Columbia and Paraguay to name but a few. This is nothing short of scandalous in a developed country.

In October 2006, ITCAN presented a study of 2300 smokers across Canada conducted by GfK Research Dynamics. The results were made available to the public, and can be found on

ITCAN's website. The main findings of the study were alarming; during the period covered by the study, 23.5% of weekly cigarette purchases in Ontario involved illicit sources. According to a later GfK study, this figure increased to 31.6% in 2007 and a further follow up study by GfK, released in August, 2008, demonstrated that the percentage of illicit trade in Ontario had increased to 48.6% of all purchases (Quebec, in second place, has an illicit market compromising just over 40% of the total tobacco market). Consequently, nearly one half of all cigarettes currently smoked in Ontario are illicit. These numbers are corroborated both by the RCMP and by health groups.

Illegal cigarettes are sold in unmarked plastic bags of 200 for as low as \$6, compared to at least \$60 for the same number of legal cigarettes. There are no health controls on illegal cigarettes. They are manufactured in illegal factories with no government oversight, no safety or content monitoring, and no labeling. This illicit trade makes a complete mockery of tobacco control.

The 2006 GfK study also revealed that at least 95% of the illicit cigarettes identified were manufactured on First Nations reserves. In addition, Health Canada's CTUM Survey revealed in 2008 that, for the first time in many years, consumption of tobacco products had increased despite the fact that sales of legal products had decreased. Groups such as the Canadian Cancer Society attribute this to the illegal cigarette trade.

The consequences of an illicit market of this size are particularly disturbing in the case of young people. An analysis carried out by GfK in 2008 of cigarette butts collected near high schools revealed that the average penetration of illegal cigarettes among adolescents was 26% in Ontario.

This was up 2% compared to 2007. This is not a phenomenon confined to the vicinity of First Nation reserves. Some of the highest percentages (close to 50% of cigarettes) are seen in municipalities like Mississauga, Newmarket and Aurora. The conclusion is inescapable: illegal tobacco is easily accessible to youth smokers throughout Ontario.

Clearly, the health and underage smoking policy objectives of the Ontario government are compromised by illicit trade. Illicit products do not comply with, and even flaunt, tobacco regulations, and those involved in illicit trade do not care about the age of their customers, making it very easy for minors to obtain illegal products at very low prices. In addition, this trade is estimated to be costing the federal government alone upwards of \$2.4 billion in annual tax revenues. Only five months ago, Ontario's Auditor General estimated that the loss to annual Ontario tax revenues from the current illicit trade in tobacco products could be as high as \$500 million.

The impact of illicit trade extends beyond the losses suffered by legal manufacturers and government revenue departments. Legitimate retailers of tobacco products, most of whom conscientiously observe the complex regulatory requirements associated with the legal sale of tobacco products, are now suffering serious financial distress as a result of customers buying from illicit traders instead of at their local store.

Finally, the illegal tobacco trade is known to be controlled by criminal networks. According to the RCMP, these networks also deal in contraband alcohol, drugs and firearms. Inevitably, the

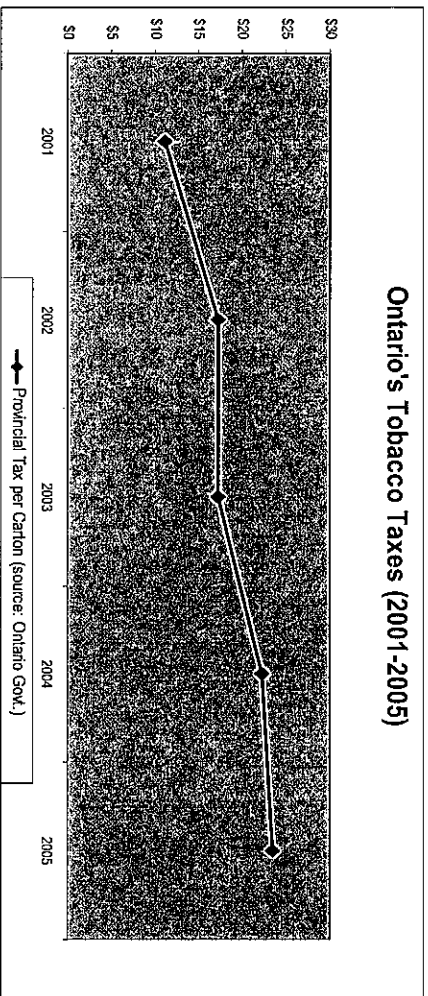
countenancing of the illicit tobacco market will only serve to increase the degree of lawlessness in Ontario generally and especially on First Nation reserves where 95% of this trade is based.

Graphical Illustrations

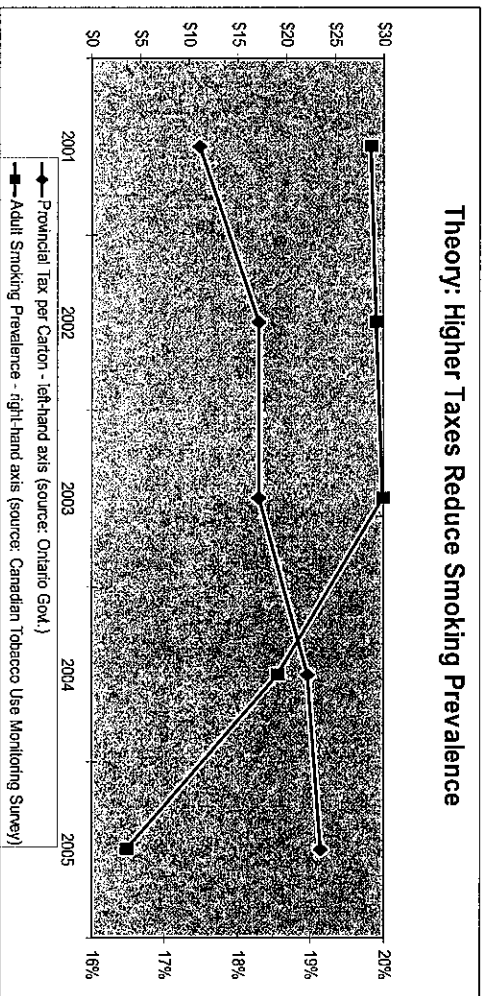
The following graphs indicate the divergence between a theory – that high tobacco taxes lead to higher government revenues and lower incidence of smoking – and the reality – that high taxes really lead to illicit trade which in turn means lower government revenues and higher incidence of smoking:

THE THEORY: 2002-2005

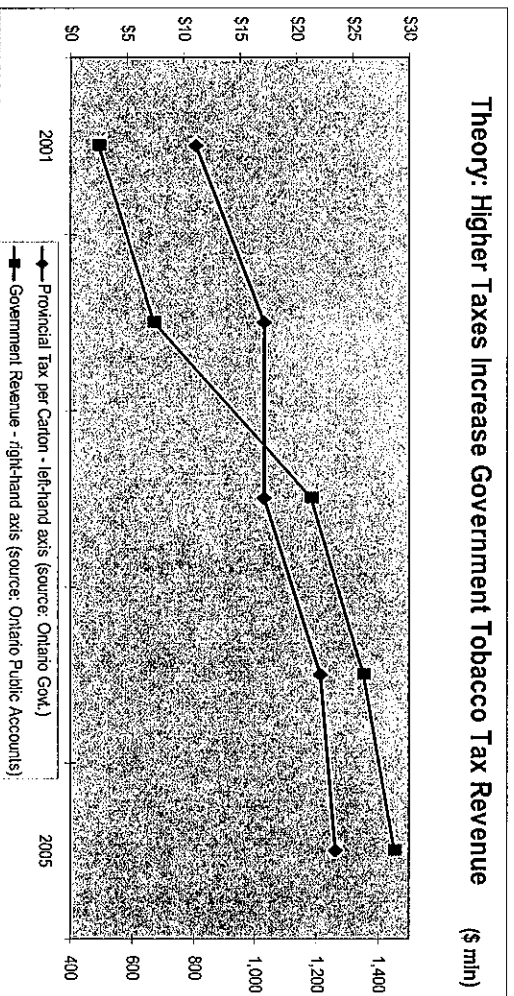
Ontario's Tobacco Taxes (2001-2005)



Theory: Higher Taxes Reduce Smoking Prevalence

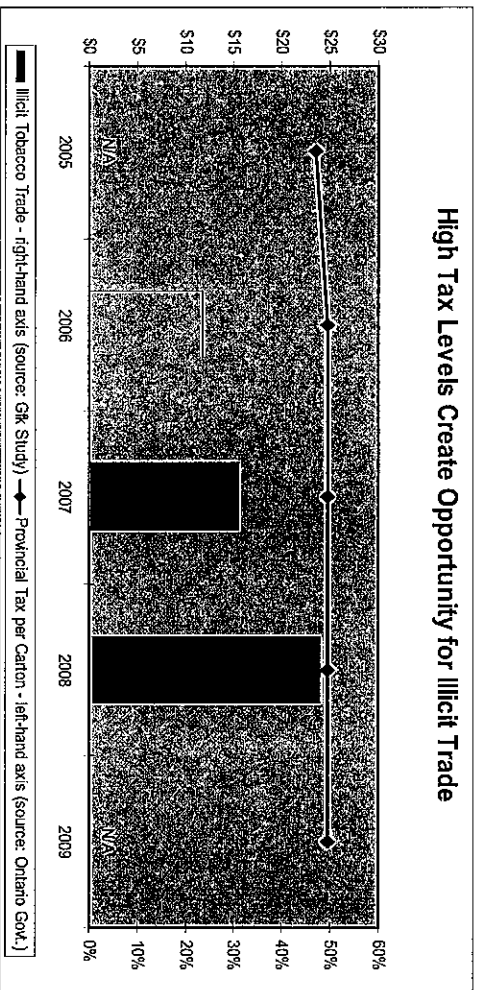


Theory: Higher Taxes Increase Government Tobacco Tax Revenue (\$ mil)

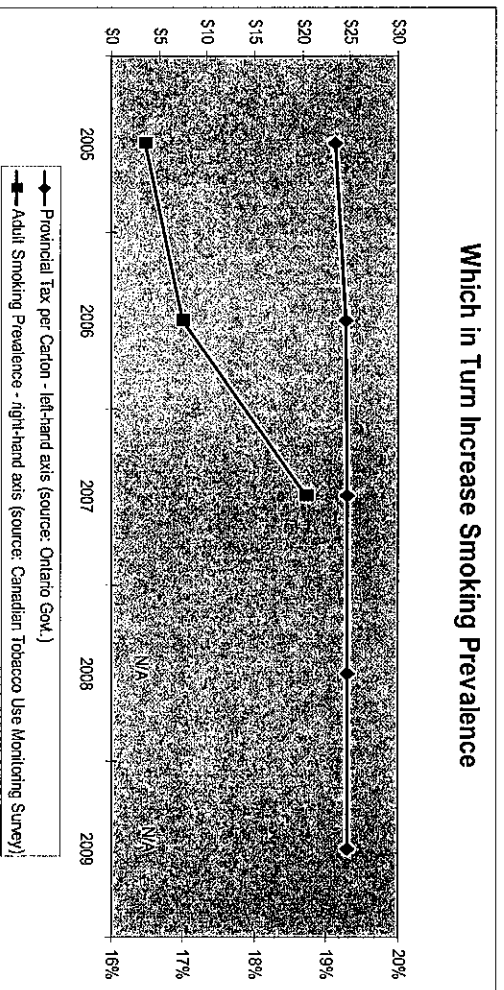


THE REALITY: 2005-TODAY

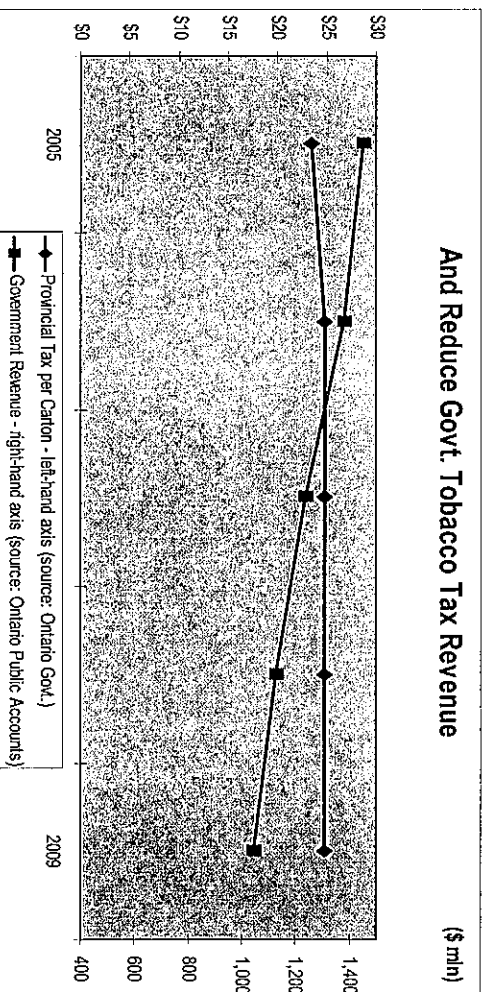
High Tax Levels Create Opportunity for Illicit Trade



Which in Turn Increase Smoking Prevalence

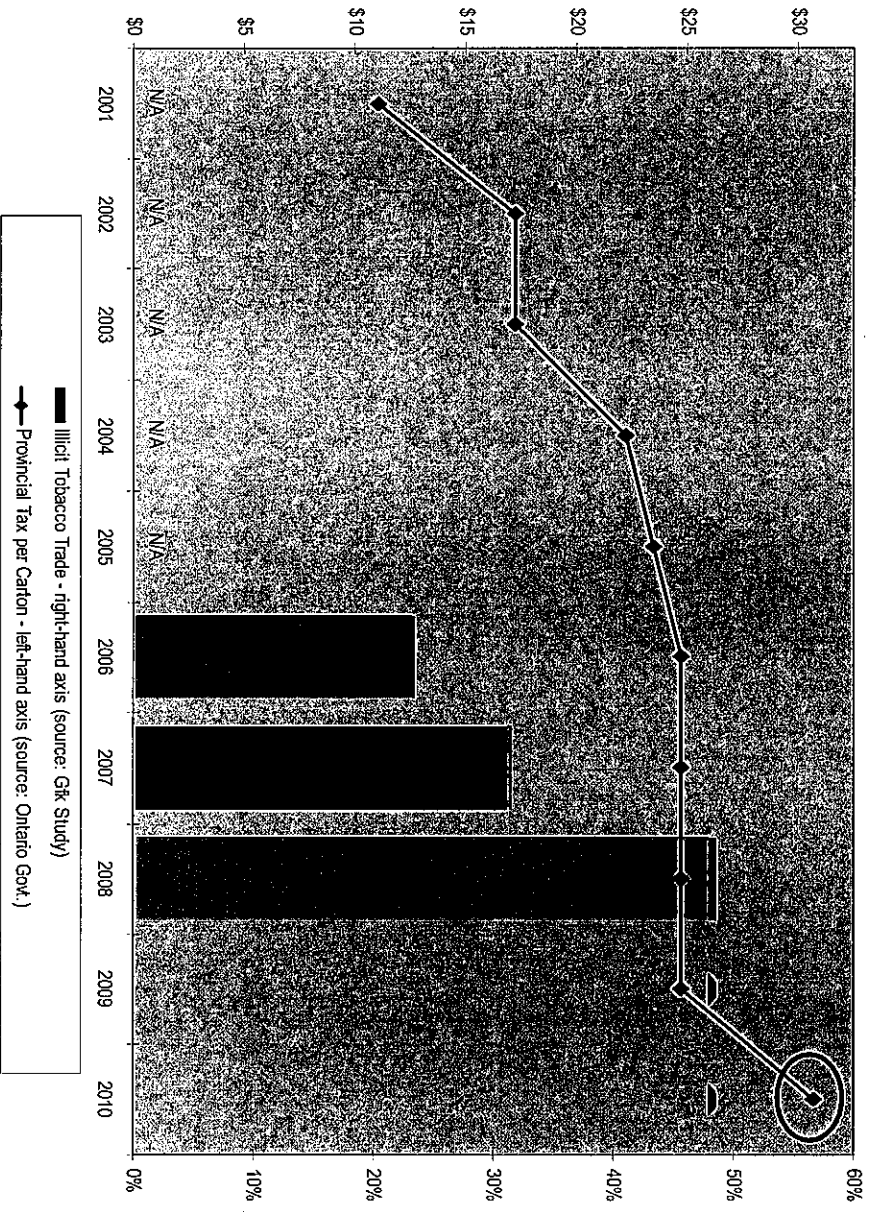


And Reduce Govt. Tobacco Tax Revenue (\$ mln)



THE FUTURE (?)

Global Economic Downturn - Ontario's Budget Deficit Response Compounding the Situation?



Note: "Provincial Tax per Pack..." includes both Provincial Tobacco Tax and the Provincial portion of value added taxes and sales taxes.
Note: Provincial Tax per Carton is as at July 1st of the relevant year.

ITCAN has sought vigorous government action, both federal and provincial on the elimination of this illegal trade. In our meetings with the federal government however it is clear that there is no effective communication between the various ministries which are affected by this phenomenon (Public Safety, Revenue, Finance, Justice, Health and Indian Affairs) and there is confusion about which department should have the lead role in handling the issue. There appears to be little communication as well between federal and provincial governments. No government seems willing to deal directly with First Nations leaders on the issue and, rather unbelievably, ITCAN is routinely asked by government officials about how First Nations themselves feel about the issue.

Our recommendation is that a national task force be created, headed by a senior federal Minister. This task force should also have representatives from those provincial governments like Ontario and Quebec most affected by the issue, as well as representatives of police agencies, First Nations leaders, health groups, those involved in the legal tobacco manufacturing trade and other interested parties. This task force should consider a number of solutions to fight the illegal tobacco trade, including:

- More effective and equitable enforcement of all relevant laws and regulation including those governing licensing, packaging, excise and tobacco control.
- Proper monitoring and control of the supply of specific machinery and raw materials associated with tobacco manufacturing;
- Introduction of a First Nations tobacco tax on products sold on reserves; and
- Better enforcement tools, which may include harsher fines and penalties for those convicted of working in the illegal tobacco trade.

Only through committed joint action of this type can the illegal tobacco trade be halted in Canada.

On the contrary, this Bill will not assist in the fight against illicit trade one iota. It will instead divert government resources that could have been used to reduce illegal activity into a quagmire of legal fees and legal wrangling that will last decades. It will impose new costs upon legal manufacturers which will make them less able to combat the illegal market with their own initiatives. And it may have the ultimate effect of bankrupting such manufacturers so that the whole tobacco industry will be turned over to an ungovernable and untaxable illegal market.

CONCLUSIONS

For the foregoing reasons, ITCAN submits that Bill 155: *An Act to permit the Province to recover damages and health care costs incurred because of tobacco related diseases and to make a complementary amendment to the Limitations Act, 2002*, should be rejected by the Legislative Assembly of Ontario as bad tobacco control policy.

ITCAN thanks the Standing Committee on Justice Policy for providing this opportunity for ITCAN to communicate its views on the Bill and looks forward to many future opportunities to engage with the government of Ontario and the Legislative Assembly on the many important issues relating to the manufacture, sale and control of tobacco products.