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FRONTIER DUTY FREE ASSOCIATION
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National Association of
Canada's Land Border Duty Free Shops

www.fdfa.ca

600 - 116 Lisgar Street, Ottawa, ON K2P 0C2
(T): 613-233-1946 (F): 613-238-3878

Laurie Karson, Executive Director

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INDUSTRY BACKGROUND

Canada's award-winning land border duty free sector was established in the early-1980's by the federal government, after extensive research to establish a sound and beneficial mandate for the sector:

- To provide economic benefit to Canada;
- To repatriate sales otherwise lost to US duty free shops and retailers;
- To bolster Canada's tourism sector as the last point of contact with departing travelers; and
- To positively reinforce the Canadian federal identity and image, both with Canadians and visitors to Canada.

ECONOMIC BENEFITS

Land border duty free shops are independently owned and operated by Canadian citizens and residents. Licensees reside in or near the border communities where the shops are located, which has served to make the shops highly attentive to local market opportunities, and maximize local investments in facilities and staff. The duty free sector directly employs approximately 1,200 Canadians. Since 60% of the shop's trade and service suppliers are located in Canada, indirect employment fostered by the sector is substantial. Total direct and indirect employment is estimated to be over 2,500 FTE Canadian jobs. Many are in border communities among the hardest hit by the economic recession.

The shops contribute approximately $35 million to annual federal, provincial and local tax rolls. Shop operators have invested over $60m in facilities, and purchase millions of dollars annually from Canadian businesses for operating supplies and services.

SHOP OPERATIONS & PUBLIC SAFEGUARDS

Travellers cross the border for business, holiday or other leisure-time activities. Duty Free Shopping is not a purpose or driver of cross border travel. The land border duty free program was established by the federal government in the early 1980's to reverse the significant loss of sales and related economic benefits, as cross border travelers chose to purchase at US duty free shops and retailers versus in Canada, due to more attractive prices in the less regulated and highly competitive US retail market.

Safeguards were put in place to ensure that duty free shopping could not be abused or result in additional loss of business to Canadian retailers. The shops are located at secure points of no return to Canada, overseen by Canada Border Services Agency. These controlled locations that are distant from the place of residence of most Canadians, are not convenient or accessible for day-to-day shopping. Typical travellers cross the border and visit the shops 1-2 times per year at the most.

Due to low US pricing cross border travellers look to US duty free shops and retailers, and not Canadian retailers, as their shopping alternative to Canadian land border duty free shops. Duty Free Shops do not cannibalize sales from provincial liquor stores. Regulatory controls and the fact that tobacco is not sold in small pack quantities ensure that duty free shops are not working contrary to Canada's overarching health strategies.

The sole impact is to re-distribute sales away from the US and illicit channels, and not to increase market size. Duty free consistently accounts for less than 1% of the Canadian tobacco market.

Duty Free Hors Taxes

It's better at the border
Économisez plus à la frontière

CURRENT GOVERNMENT POLICY CHALLENGES

Taxation of Duty Free Shops

The 2014 budget announcement of a $6 excise tax increase on duty free tobacco purchases, equalizing the tax with domestic retail, is a misguided and counterproductive change that will damage our competitiveness and do nothing to support Canada's overarching tobacco health strategies. This change was made without industry consultation, and appears to have been done with no regard to the well grounded federal land border duty free program mandate. The change will serve to divert sales to uncontrolled U.S. and illicit retail channels.

Established safeguards, combined with the fact that licensees do not sell tobacco products in single pack quantities, ensure that duty free shops do not influence nor attract sales from new smokers, those intending to quit smoking, or youth. Due to the degree of control and perceived government oversight, underage smokers are far less likely to attempt making purchases at duty free shops versus at illicit outlets or convenience stores. The sole impact of duty free shops is to re-distribute sales away from the US and less controlled retail channels. The sector is therefore not in conflict with Canada's overarching health strategy, and should not be targeted by misguided regulatory changes.

The taxation of duty free tobacco purchases began in 2002, when tobacco smuggling was a major problem and focus. This was done to appease unfounded concerns of some policy makers that low duty free prices could make the industry a target for would-be smugglers. At the time law enforcement officials determined that duty free had no credible links to illicit activity. Our sector cooperated with decision makers at the time who recognized the tax was a symbolic gesture, rather than an effective anti-smuggling measure. The negative financial impacts on duty free businesses were partially offset by the concurrent elimination of duty free shop licensing fees, a differential left between the tax charged duty free shops versus domestic retailers, and government commitments to have CBSA collect the tax on US bought tobacco imports by individuals. CBSA has never effectively implemented this final commitment. The 2014 budget change is therefore seen as a counterproductive and unfair targeting of our sector. We seek government consultations to discuss this matter and ensure this practice will not continue. Duty Free tobacco unit sales are consistently less than 1% of the Canadian market and have declined by 45-50% since 2002, showing the industry is not running contrary to Canada's health strategy (industry sales declines are far outpacing reported tobacco consumption declines of ~30%).

Provincial Liquor Board Pricing & Restrictive Trade Practices

Federal regulations require duty free shops to purchase alcoholic beverages based on agreements with provincial liquor boards. The boards charge excessive mark-ups and have instituted overreaching terms affecting purchase costs, sale prices and other practices that are increasingly eroding our competitiveness in a highly price sensitive "export" sector, characterized by informed and empowered consumers. Alternatively, our US retail and duty free competitors are able to purchase directly from alcoholic beverage manufacturers at significantly lower cost, and have greater flexibility in establishing pricing and promotional programs. Discussion with federal policy makers is needed regarding how the legal & regulatory framework needs to evolve, so our industry can continue to successfully fulfill its' mandate.

Canadian versus U.S. Product Labelling Requirements

Different product labeling standards between the US and Canada threaten to eliminate commodities from Canadian duty free shelves, while US duty free shops and retailers can continue to sell them. Canadian land border duty free shops cannot sell U.S. tobacco purchased by Americans and some liquor products for export to the US, even though the labeling fully complies with US requirements. At the same time these items if purchased in the U.S. can be imported into Canada by consumers, even though the labeling does not meet Canadian requirements. The industry seeks meaningful consultations with government, to find a reasonable and effective means to deal with these issues and protect our competitiveness.

Credit Card Discount Fees

Banks and credit card companies must be legislated to directly charge their customers for perk card benefits. Interac processing is an essential retailer service, and must be subject to a fixed maximum discount fee for secure processing of transactions. Charging excess fees for perk cards is a matter between banks/credit card issuers and their customers, and should not be lumped in with the Interac discount rate. It is unreasonable and impractical to expect retailers to manage collection of differential perk card fees on the large number of card types.

Customs Allowances

The Federal Government made positive changes to Canada's Customs allowances effective June 1, 2012. Further evolutionary changes are warranted such as creating exemptions on wine and beer purchases, based on a 24-hour absence from Canada. Creating some allowance for those travelling <48 hours away (perhaps due to affordability) would be positively received by the public. It would also give duty free operators the ability to sell more Canadian-made beer, wine and Ice Wine – by redistributing additional sales away from US competitors.