

The status of the illicit tobacco trade in the Eastern Mediterranean Region



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Terms

Contraband refers to products diverted into illicit trade, not respecting the legal requirements in the jurisdiction of destination.

Illicit trade means any practice or conduct prohibited by law and which relates to production, shipment, receipt, possession, distribution, sale or purchase, including any practice or conduct intended to facilitate such activity.

Smuggling is one type of illicit trade and refers to products illegally traded across borders; the illegal crossing of borders between jurisdictions being a key characteristic.

Illicit manufacturing is another type of illicit trade and refers to the production of tobacco products contrary to law. One form of illegal manufacturing is **counterfeit tobacco production** in which the manufactured products bear a trademark without the consent of the owner of the trademark. Illegally manufactured products can be sold on the domestic market or smuggled into another jurisdiction.

Tracking and tracing means systematic monitoring and re-creation by competent authorities or any other person acting on their behalf of the route or movement taken by items through the supply chain.

The size of the illicit cigarette trade in the Eastern Mediterranean Region

Measuring illicit cigarette trade is methodologically challenging for many reasons. Such trade is an illegal activity and illegal traders are unlikely to record their activities. For security reasons, data on illicit trade are usually difficult to collect, as law enforcement agencies often prefer not to publicize the scope of their activity. All methods to estimate illicit trade have their limitations and not all studies clearly describe their methodology or these limitations.

Transparent and public data on illicit tobacco trade are missing in most countries of the Eastern Mediterranean Region and are not available in the reporting instruments of the WHO Framework Convention on Tobacco Control (WHO FCTC) for the countries of the Region. Exceptions are Pakistan and the Islamic Republic of Iran. Although no official surveys are available in Pakistan, it is estimated that almost 17% of the total domestic market of cigarettes is illicit which includes smuggled, counterfeit and non duty paid locally manufactured products. Out of this some independent researchers have quantified smuggled cigarettes as 5% of the total domestic market (Source: Federal Board of Revenue, 2012). In the Islamic Republic of Iran, a study by researchers at the country's Tobacco Control and Prevention Research Center found that 21% of all cigarettes on the market in Teheran in 2009 were illicit.¹

According to Euromonitor, the share of illicit in total cigarette consumption in Tunisia increased from 12% in 2008 to 28% in 2013, peaked at 24% in Egypt in 2012 and was more than 20% in the United Arab Emirates in 2013.² It is likely that political unrest, conflict and reduced border security have facilitated illicit tobacco trade in parts of the Region.

The World Customs Organization collects data on tobacco product seizures around the world. Although data from some

countries are missing, the global share of cigarette seizures in the Middle East in 2012 was rather low (less than 1% of all seized cigarettes globally).³ The low figure for the Middle East can be explained by the low level of seizures and by the low level of reporting of such seizures to the World Customs Organization.

In terms of other tobacco products, the World Customs Organization noticed a significant increase in 2013 in the quantity of chewing tobacco seized, which in 2012 amounted to 7997 kg compared to 37 844 kg reported in 2013, reflecting an increase of nearly 5 times. An increase in figures from 2011 to 2012 had already been noted.

For waterpipe tobacco, a significant increase in the number of seizures has been observed; however this increase is not reflected in the total quantity seized (75 056 kg in 2013) due to the small quantities seized (i.e. 1 kg or less), which was not the case in 2012.⁴

The effect of eliminating illicit tobacco trade

The availability of inexpensive, illicit cigarettes increases consumption and the risk of premature deaths due to tobacco use. Eliminating or reducing this illicit trade helps to reduce consumption by increasing price and reducing premature deaths. Consumption would fall if illicit trade were eliminated because in most countries, illicit cigarettes are much less expensive than their legal, fully taxed equivalent. As illicit trade is reduced, the overall average price of cigarettes goes up, and consumption consequently goes down.

Illicit tobacco undermines the effectiveness of tax policies, leads to over US\$40 billion in lost revenue globally and increases the availability of inexpensive cigarettes. If the global illicit trade were eliminated, governments would gain at least US\$ 31 billion in income and from 2030 onwards over 160 000 lives a year would be saved.⁵

The role of the tobacco industry in illicit trade

Evidence of the direct and indirect involvement of the tobacco industry in cigarette smuggling is well documented, on the basis of internal documents,⁶ its own admission⁷ and court judgements.⁸ According to research on internal documents, evidence of the complicity of transnational tobacco companies in cigarette smuggling extends to Lebanon and the Middle East, where this trade has benefited from weak governance and chronic political instability.⁹ In 2000, the deputy chairman of British American Tobacco (BAT) admitted: “Where any government is unwilling to act or their efforts are unsuccessful, we act, completely within the law, on the basis that our brands will be available alongside those of our competitors in the smuggled as well as the legitimate market.” In July 2008 and April 2010, three tobacco companies in Canada pleaded guilty and admitted “aiding persons to sell or be in possession of tobacco products manufactured in Canada that were not packaged and were not stamped in conformity with the Excise Act” while Northern Brands International Inc., a company related to RJR, pleaded guilty to a conspiracy offence under the Criminal Code.¹⁰ Since 2004, the four major international tobacco companies have paid billions of dollars in fines and payments to settle cigarette smuggling litigation in Europe and Canada. (Europe: Philip Morris International and Japan Tobacco International = US\$ 1.4 billion;¹¹ Canada: Imperial Tobacco Canada Ltd., Rothmans, Benson & Hedges and JTI Macdonald = US\$ 1.7 billion).

An ongoing lawsuit in the European Union accuses RJ Reynolds (RJR) of running a global money laundering scheme with organized crime groups that involved the smuggling of drugs and cigarettes.¹²

In 2012, a major tobacco company, Japan Tobacco International (JTI), was accused of smuggling activities in the Middle East and

under official investigation of the European Anti-Fraud Office, OLAF.¹³

According to the investigative journalists of the Organized Crime and Corruption Reporting Project, internal JTI records revealed the following.

- “Smuggling incidents were reported almost monthly during 2009-10, but former employees said no action was taken in the company’s most profitable areas. Investigators suspected tens of millions of JTI cigarettes were being diverted to smuggling operations in the Philippines, Afghanistan, Jordan, Iraq and elsewhere, often with the help of JTI’s own distributors.
- When investigators received information that 13 JTI employees or distributors may have been working directly with smugglers, a senior JTI vice president blocked an investigation, according to company e-mails and internal memos.
- JTI contractors paid officials in Iraq, Kurdistan and Iran to get information on smuggling routes, according to company internal reports and interviews with contractors.”¹⁴

Tobacco industry claims

The tobacco industry has claimed that high taxes drive smuggling and has sometimes argued successfully to governments that they should not increase tobacco tax because this will increase the level of smuggling. The argument is that smugglers will smuggle into a country where they can make the highest profit, and that these are the countries where tax is a high proportion of the price, leaving a large margin to reduce the price (by evading tax) and still retain a profit. In fact the overall level of smuggling is generally higher in countries that have lower cigarette prices (generally also countries also with a lower tax rate) than in

countries that have high prices. Although a high tax margin may provide the initial incentive to smuggle, the data show that it is not the only factor. Other important factors include the ease and cost of operating in a country, industry participation, how well organized crime networks are, the likelihood of being caught, the punishment if caught, corruption levels and so on.¹⁵

It is an established practice for the tobacco industry to use illicit trade as the main argument against higher taxes and product regulation as part of a public relations campaign with a focus on the following strategic messages.

- We don't condone cigarette smuggling, but are rather a victim of it.
- Illicit cigarettes contain many toxic ingredients and harm our reputation.
- High taxes are the main cause of smuggling.
- Product regulation, such as plain packaging or a ban of menthol cigarettes, will further increase illegal trade.
- We are willing to combat illicit trade and to collaborate with governments.
- Joint action of the tobacco industry and governments is best consolidated in agreements.
- We commission research to know the scope of illicit trade.
- Increasing and high levels of smuggling are convincing arguments to combat higher taxes or product regulation.
- Traceability should be the responsibility for the industry.
- The real concern are counterfeit cigarettes and 'illicit whites', not the smuggling of genuine products

Most of the reports on illicit trade levels are commissioned by cigarette manufacturers. Growing evidence shows that the industry tends to overstate the illicit cigarette trade problem.¹⁶ The aim of the illicit trade strategy of the tobacco companies is to prevent legislation, to collaborate with governments and to provide anti-smuggling solutions which remain under their control.

The Protocol to Eliminate Illicit Trade in Tobacco Products

The global scope and multifaceted nature of the illicit tobacco trade requires a coordinated international response and improved global regulation of the legal tobacco trade.

Illicit tobacco trade is addressed in Article 15 of the WHO Framework Convention on Tobacco Control (FCTC) and by the Protocol to Eliminate Illicit Trade in Tobacco Products (ITP). In the preamble of the WHO FCTC it was recognized that “cooperative action is necessary to eliminate all forms of illicit trade in cigarettes and other tobacco products, including smuggling, illicit manufacturing and counterfeiting.” Article 15 of the WHO FCTC addresses illicit trade in tobacco products and stipulates in its first paragraph that “the elimination of all forms of illicit trade in tobacco products (...) are essential components of tobacco control.” The ITP has been negotiated as a supplementary treaty to the WHO FCTC. The ITP, adopted at the fifth session of the Conference of the Parties in November 2012, will enter into force on the 90th day following the 40th ratification of the Protocol. Only Parties to the Protocol will be bound by its obligations. After 22 months, 54 Parties to the WHO FCTC (including 8 States from the Eastern Mediterranean Region) have signed, and four States (Nicaragua, Uruguay, Gabon and Mongolia) have ratified the Protocol. Enforceable measures to control the supply chain and international cooperative

measures, including information sharing and cooperation in the investigation and prosecution of offences, are at the heart of the Protocol.

It contains detailed provisions on licensing, record keeping, tracking and tracing, due diligence, control of free zones, traceable methods of payment, international cooperation and monitoring.

One of the core measures of the Protocol is a global tracking and tracing regime (Article 8). The aim of the tracking and tracing system is to assist in the investigation of illicit trade of tobacco products. According to this article, each Party shall require that unique, secure and non-removable identification markings, such as codes or stamps, are affixed to or form part of all unit packets, packages and any outside packaging of cigarettes within a period of five years, and of other tobacco products within a period of ten years of entry into force of the Protocol.

Article 8 of the Protocol specifically notes the need to avoid delegating tracking and tracing to the tobacco industry.

“12. Obligations assigned to a Party shall not be performed by or delegated to the tobacco industry.

13. Each Party shall ensure that its competent authorities, in participating in the tracking and tracing regime, interact with the tobacco industry and those representing the interests of the tobacco industry only to the extent strictly necessary in the implementation of this Article.”

The way forward

Transnational organized crime markets are global in scale; therefore strategies to address them should also be global.¹⁷ Case studies around the world¹⁸ show that a combination of measures such as international cooperation, legislative measures to control the supply chain and more investment in enforcement and dissuasive penalties can lead to positive results in tackling

large-scale smuggling. The only real option for international cooperation is the Framework Convention on Tobacco Control and its Protocol to combat the illicit trade in tobacco products.

However, many Parties lack expertise in the technical matters of the ITP provisions and need technical assistance. To support Member States in this area, a decision was taken by the sixth Conference of the Parties in October 2014 to establish a committee of experts to provide technical and legal advice on those matters to Parties upon request.

Another concern in the Region is illicit manufacturing. Besides raw tobacco, cigarette papers and acetate filter tow are main components for manufacturing illicit cigarettes. Although cellulose acetate has several industrial uses, acetate tow is used in very few products. More than 80% of world production is used in the manufacture of cigarettes. There are also only a handful of companies worldwide that manufacture acetate tow; seven are members of the Global Acetate Manufacturers Association.¹⁹

In 2014 the secretary-general of Interpol, Ronald K. Noble, raised the issue of “acetate tow” and illicit manufacturing and said that acetate tow was being exported in high volumes to cigarette manufacturers, “well above” the requirements for legitimate production. According to Noble, several measures should be put in place to deter the flow of acetate tow to illegal manufacturers. One of them is for governments to impose severe criminal sanctions or civil penalties on producers who knowingly sell to manufacturers producing illicit cigarettes, or who remain willfully ignorant to the final distribution points of their products. Noble finally declared that international protocols concerning tobacco-related products are being implemented but called on governments to start taking control of the supply chains of the components.²⁰

During the negotiations on the ITP, the issue of key inputs was discussed at length and it was agreed that: “Five years following

the entry into force of this Protocol, the Meeting of the Parties shall ensure at its next session that evidence-based research is conducted to ascertain whether any key inputs exist that are essential to the manufacture of tobacco products, are identifiable and can be subject to an effective control mechanism. On the basis of such research, the Meeting of the Parties shall consider appropriate action.” (Article 6, §5) It is likely that the measures against illegal manufacturing will be part of the upcoming illicit trade agenda.



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