



Towing the Line: Controlling Key Inputs to Disrupt Illegal Tobacco

MacDonald - Laurier Institute
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Cellulose Acetate Tow

- Can't make filtered cigarettes without it
- Supplied by only 6 companies: Celanese, Daicel Eastman, Mitsubishi, Rhoda Acetow and Sichuan Push Acetati Co. Ltd. (2 dominate: Eastman and Celanese)
- They oversupply, selling to illicit manufacturers in huge numbers
- In 2005, GAMA started "Know Your Customer Certificate" (KYC) Program, but not transparent or enforceable

EASTMAN

 **Celanese**



ITTP: Size & Harms

- Harms to consumer health
- Harms to brand integrity
- \$81 billion a year funds criminals and VEOs
- EU alone lost \$12.5 billion in tax revenues in 2012
- Replacing ITTP with licit would result in an additional \$31.3B in tax revenue worldwide
- Illicit averages 11.6% worldwide:
 - 16.8% in poor countries
 - 9.8% in high-income countries

CTP of ITTP

- In Sahel, same routes for drugs and tobacco
- Hezbollah: Operation Smokescreen & Operation Tobacco Road
- PKK: smuggles into Iraq in same route used by Husseins
- Real IRA fed by Belarussian smuggling gangs
- 2nd to heroin for Taliban

Key Source and Destination Markets for Illicit Cigarettes



Belarus

- Trade data for mid-2012 to mid-2013 shows Belarus imported 30,715 metric tons of tow: nearly 10 x needed for domestic production
- Celanese's supply alone exceed Belarus' own production quotas by 5 billion cigarettes
- Eastman alone sold Belarus 9.18 x requirement to satisfy national production quota
- Even allowing for declared exports, there is enough for 209 billion illicit cigarettes

Belarus's Unaccounted Tow

Year	National Quota (in B of sticks)	Filtered (in B of sticks)	MT of tow required	MT of tow imported
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2013

33

31.68

3,960

30,715.861

Paraguay

- 189 billion cigarettes can be from the tow oversupply entered the Paraguay - Argentina FTZ: Mercosur + TBA
- Registered tobacco companies in Paraguay ballooned from 3 in 1993 to 33 in 2004: a 900% industry expansion in 11 years
- 2000-2010: production increased +2,592.3% while consumption shrank -6.9% for same period

Scale of Paraguay's Illicit Production

Year	Total Production (B of sticks)	Of Which, Filtered (in B of sticks)	MT of tow required	MT of tow likely imported	Likely illicit production (B of sticks)
2011	30	27	3,375	32,306.384 (Par: 55.385 + Arg: 32,251)	231.451

UAE

- UAE's domestic consumption is all imported; its production is only for export
- 40 FTZs conceal reliable trade data of quantities and destinations
- UAE is importing 177 x the quantity of tow needed to produce its stated exports: enough to produce 98.7 billion illicit cigarettes

UAE's Excessive Tow Imports

Year	Export Production (B of sticks)	Of Which, Filtered (B of sticks)	MT of tow required for export production	MT of tow imported	Possible Illicit Production (B of sticks)
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2011	0.55	0.55	68.77	12,226.79 4	98.7
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International Legal Framework

- UK's NCA Programme 9: focused on “upstream” elements: employees of pharma companies
- INTERPOL Sec. Gen. Ron Noble on 5 March 2014: a “major enabler” of IT & “enormous source of funding” for TOCs
- WHO FCTC's Illicit Trade Protocol (2012): supply chain security, including key inputs (but only 5 years later)
- UNTOC, UNCAC, RICO, OSCO, CTF, White House Strategy to Combat Transnational Crime
- FATF International Standards on Combating Money Laundering and the Financing of Terrorism and Proliferation

Proposed Solution

- Writing into OECD policy: better supply chain control of key inputs (based on OECD' Conflict Minerals Guidance & Guidelines for Multinational Enterprises — 42 signatory countries)
- A clearinghouse with a credible authority
- INTERPOL enforcement of infractions



Clearinghouse Functions

- Regulate: institute a risk-based due diligence system to prevent adverse impact
- Punish & Reward: brands can promote their CSR; non-compliant are named-and-shamed
- Educate: consumers & LEA
- Coordinate: diverse international actors & authorities

Clearinghouse Operations

- Define legal market of each tobacco & filter manufacturer in every market
 - Sales / tax data of previous year (+ x% margin)
 - Supported by KPMG, PWC, WCO, etc.
- Two manufacturers clear each order / shipment through clearinghouse
 - No shipment beyond legal market demand
 - Stock keeping / inventory allowed, but must be recorded and audited by clearinghouse

Regulatory Solutions

- Certification of buyers, sellers, exporters, agents and manufacturers involved in the sale of tow (start with high-impact hot spots, where > 40% of IT is)
- Clearinghouse by competent authority to ensure that tow shipments are in line with legal market demand for each tobacco manufacturer
- Effective tracking-and-tracing: in-bale RFID chip

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