PHILIP MORRIS LIMITED

Submission to the Parliamentary Joint Committee on Law Enforcement

Inquiry into Illicit Tobacco

27 November 2019

Philip Morris Limited (PML) welcomes the opportunity to make an additional submission to the Parliamentary Joint Committee on Law Enforcement inquiry into illicit tobacco.

In early 2016, PML provided a submission to this inquiry under the 44th Parliament (provided as Attachment A). Our previous submission details our response to the Committee's terms of reference. This current submission provided updates and new information further to our earlier submission and we respectfully request they be considered together by the Committee along with all other evidence provided.

Recent Reforms

At the outset, we wish to highlight and commend the Australian Government and Parliament on a series of significant, bipartisan reforms that have impacted the illicit tobacco over the last few years, including:
- The formation of the multi-agency Illicit Tobacco Taskforce;
- New legislation which provide for fault-based offences and reasonable suspicion offences;
- Permit requirements for tobacco importers; and
- Changes to tax tobacco at the border.

Our commitment: doing our part to put an end to illicit trade

Philip Morris International (PMI), our parent company, is a leading international tobacco company, with six of the world's top 15 international brands. Our goals are to provide high quality and innovative products to adult smokers, and reduce the harm caused by smoking while operating our business sustainably and with integrity. We aim to reduce the harm caused by smoking through supporting effective evidence-based regulation of tobacco products and through our investment in developing products with the potential to reduce the risk of tobacco-related disease.

Illicit trade in tobacco hurts our business, exposes consumers to substandard products which do not comply with regulations, robs governments and taxpayers of needed tax revenues, takes business away from legitimate retailers, and helps fund criminal organisations. According to the World Health Organization (WHO), it is estimated that one in every 10 cigarettes and tobacco products consumed globally is illicit and that the illicit market is supported by various players, ranging from petty peddlers to organised criminal networks involved in arms and human trafficking.[1]

The illicit tobacco trade is widely acknowledged not only by the WHO, but governments, law enforcement agencies, and public health authorities around the world, along with the legitimate industry as a serious and complex problem, with broad and dangerous consequences. Calls for joint action and a multi-sector approach to eliminate this illegal activity are virtually unanimous and echoed by many.

Fighting illicit trade is a top priority for PMI. We are firmly committed to doing our part in the fight to eliminate the illicit tobacco trade. The stakes are high, and the threat to our business from the criminals behind this illegal activity is real. We sell our products in more than 180 countries around the world, including Australia. It makes reputational and business sense for us to ensure that our products are legally sold in the markets for which they are intended.

We are a business with genuine interests to protect and advance in opposing, disrupting, and preventing the illicit tobacco trade. Our reputation is invested in being a responsible corporate

---

[1] https://www.who.int/news-room/fact-sheets/detail/tobacco

citizen with a commitment to demonstrating this in high level strategic and everyday actions, and our company's dedication to ethical conduct and regulatory compliance.

Moreover, our commitments and investments in combatting illicit trade make good business sense. We lose revenue and market share due to the illegal tobacco trade. Every time an adult smoker in a high-price market such as Australia buys one of our premium brands smuggled from low-price markets, we lose multiples of the revenue we could have earned if the product had been sold in the intended market of sale.

Measurement of Illicit Tobacco in Australia

Tobacco products are among the most illegally trafficked goods in the world. The global black market is large and growing. PML and Imperial Tobacco Australia (ITA) commission KPMG UK to estimate, on an annual basis, the size of the illicit tobacco market in Australia. (Attachment B)

The purpose of this annual report is:
1. To provide an overview of the nature and dynamics of the legal and illicit tobacco markets in Australia, and
2. To provide an independent estimate of the size of the illicit tobacco market in Australia.

The 2018 Full Year Report reveals 2.1 million kilograms of illicit tobacco were consumed last year, representing 14.1% of the total tobacco market. If this illicit tobacco had been consumed legally, it would have represented an estimated excise value of AUD 2.02 billion.

Other key findings of the report are:
- Contraband consumption accounted for the majority of total illicit consumption, increasing from 51.1% in 2017 to 53.7% of the total illicit consumption in 2018.
- Unbranded, or "chop chop" tobacco consumption accounts for 44.4% of total illicit consumption.
- Australia has the highest cigarette prices within the Asia Pacific region.
- The price differentials between legal and illicit products has widened.

Involvement of Organised Crime

"Tobacco is one of the most highly taxed commodities in Australia and across the world, which makes illicit tobacco an attractive market for organised criminal syndicates."[2]

The Australian Criminal Intelligence Commission (ACIC) Annual Report 2017-18 stated, "Tobacco is one of the most highly taxed commodities in Australia. Serious and organised crime groups find it attractive, as lucrative profits can be made through tax evasion and most of these profits are channelled back into organised crime."[3]

Smugglers diverting contraband from their intended market, producing counterfeits or illicit white cigarette products cheaply, and smuggling them in Australia can make huge profits. Just one container of illicit cigarettes smuggled from the Middle East or South-East Asia could generate easily generate over $5 million in profit once landed and in the market in Australia. Following the Operation Minium seizure of nine million illicit Manchester cigarettes by the Polaris Joint Waterfront Taskforce announced on 30 September 2015, the law enforcement agencies involved advised:

---

[2] The Hon Angus Taylor MP, Minister for Energy and Emissions Reduction in his former role as Minister for Law Enforcement and Cyber Security, http://ministers.treasury.gov.au/ministers/kelly-odwyer-2016/media-releases/combating-illicit-tobacco-0
[3] https://www.acic.gov.au/feature-targeting-illicit-tobacco

> *"The cigarettes have a black market value of approximately $5.4 million and it will be alleged the illegal importation would have avoided tobacco excise and Customs duties of about $4.77 million."[4]*

In July 2018, a joint investigation involving officers from the Australian Border Force (ABF), the Department of Home Affairs, the ACIC, the Queensland Police Service, and NSW Police Force resulted in the seizure of almost 60 million cigarettes, representing more than AUD 40 million in evaded duty. In announcing the seizures, ACIC Queensland State Manager Charlie Carver said serious and organised crime groups are more attracted to the Australian illicit tobacco market than ever before.[5]

The 2018-19 financial year saw eight seizures, down from 19 during the previous financial year. While 41,000 kilograms of illegal tobacco were confiscated and destroyed during this period, there were only four convictions[6]. We acknowledge recent legislative reforms which increased the range of options available for illegal tobacco offences and hope to see these powers deliver further prosecutions.

Taxation

Taxation plays a determinative role in broad-based public health policy in reducing smoking rates. However, excise tax increases, that are dramatically out of step with the consumer price index (of the legal regulated market), have shown to enable (untaxed) black markets and embolden criminals.

The Federal Government's Black Economy Taskforce handed down its report[7] in May 2017. The report noted, "As a result of excise increases, tobacco in Australia is currently more valuable by weight than silver. This makes it very profitable to deal in illicit tobacco."

Australian cigarettes are already the most expensive in the world. Since 2012, the price of cigarettes has risen by, on average, 40% after the Government introduced annual 12.5% tobacco excise increases.

If tobacco excise increases are continued in their current annual increments, it will significantly undermine the public policy objectives that tobacco excise is designed to achieve and will give rise to further increases in illicit trade and theft. Australia already ranks as the second highest Organisation for Economic Co-operation and Development (OECD) member for tobacco tax levels with a 68.4% excise incidence level.

We note the New Zealand Tax Working Group Future of Tax final report[8], issued in February 2019, which states, "The Group's preference is that, once the current schedule of tobacco excise increases end, the Government prioritise other measures to help people stop smoking before it considers further large increases in tobacco excises." The Working Group's interim report[9], also outlined concerns about further tobacco excise increases for the following reasons:

1. Tobacco excise is regressive. There is a substantially higher prevalence of smoking in the poorest areas of our country (New Zealand Health Survey 2016/17). Although increases in the rates of

---

[4] https://newsroom.abf.gov.au/releases/thirteen-charged-illegal-tobacco-importation-syndicate-shut-down-polaris-joint-waterfront-taskforce?mode=print

[5] https://www.acic.gov.au/media-centre/joint-media-releases/57-million-illegal-cigarettes-seized-joint-operation

[6] https://www.ato.gov.au/General/The-fight-against-tax-crime/Our-focus/Illicit-Tobacco/

[7] https://treasury.gov.au/sites/default/files/2019-03/Black-Economy-Taskforce_Final-Report.pdf

[8] https://taxworkinggroup.govt.nz/sites/default/files/2019-03/twg-final-report-voli-feb19-v1.pdf

[9] https://taxworkinggroup.govt.nz/sites/default/files/2018-09/twg-interim-report-sep18.pdf

excise may encourage some individuals to cease smoking, the heaviest burden of the excise increases will be borne by low-income earners who continue to smoke.

2. The effectiveness of excise increases appears to be reducing. Regulatory impact analysis prepared by the Treasury in 2016 indicates that reductions in smoking prevalence are expected to be quite small relative to the size of the increases in the excise rates (Treasury 2016).

3. High taxes on tobacco appear to be a factor in an increasing number of robberies and criminal activity.

ACCC application

In August 2016, PML, British American Tobacco Australia, and ITA sought authorisation from the Australian Consumer and Competition Commission (ACCC) to jointly cease supply to retailers and wholesalers caught selling illegal tobacco.

The purpose of the application was to deter and minimise the supply of illicit tobacco products at the retail level with the application seeking authorisation, in accordance with a defined process, to suspend or cease supply to retailers or wholesalers found to be supplying illicit tobacco products.

It was a disappointing decision for the ACCC to reject our application to jointly act against the illegal tobacco trade in Australia. The three tobacco companies are in a unique position to take coordinated action against those retailers and wholesalers who sell black market tobacco. We believe that removing the ability of retailers and wholesalers to acquire and supply legal tobacco would be a strong disincentive to trade in illicit products.

While the ACCC rejected the industry's proposed action, it readily acknowledged that "illicit tobacco is a problem that undermines public health policies and diverts revenue from legitimate retailers and government," and commented on the desirability of additional Government action to address it.

State Law Enforcement

The retail selling of tobacco is administered by the states and territories. Whilst most states and territories have powers under respective laws to enforce laws against the selling of illicit tobacco and to sanction illicit actors, very little action is taken. New South Wales and Victoria have been particularly proactive on this front, with a Penshurst (NSW) retailer receiving a fine of AUD 80,000 for selling illegal cigarettes[10].

In August 2019, the Geelong Advertiser reported that Geelong Police had seized more than 500 kilograms of "chop chop" tobacco, worth about AUD 550,000, from a storage facility[11]. This seizure followed a police raid on a store in central Geelong where they discovered in excess of 88,000 illegally imported and homemade cigarettes.

While we welcome these actions, more needs to be done to penalise the selling of illicit tobacco, particularly in the states where legislation is limited or unclear. The Commonwealth should consider how to urge all State and Territory Governments to strengthen existing legislation around the retail selling of illicit tobacco and encourage law enforcement authorities to actively enforce that legislation.

---

[10] https://www.theleader.com.au/story/6273620/penshurst-retailer-burnt-with-major-tobacco-bust/
[11] https://www.geelongadvertiser.com.au/news/crime-court/geelong-police-abf-agents-seize-500kg-tobacco-from-north-geelong/news-story/3181ac5800b604e17a35bf08302d566f

Overseas Developments

According to the WHO, the global illicit tobacco trade is valued at approximately USD 40 billion annually; more than the illicit trade in oil, wildlife, timber, arts and cultural property [antiquities], and blood diamonds combined. Terrorist networks and transnational organised crime syndicates are using proceeds from the illicit tobacco trade to finance their operations. Not only does this compromise global security, it costs governments billions in lost revenue and poses a greater health risk to consumers. As criminals identify optimal – and profitable routes – to smuggle illicit tobacco, offenders easily adapt the methodology to smuggle guns, drugs, and people. There is evidence of this convergence in countries all over the world.

Globally, governments have been working on finding solutions to this threat. Many of the examples provided below highlight the strong commitment to tackle the issue.

I.   WHO FCTC Protocol to eliminate illicit trade of tobacco products [12]

The WHO Framework Convention on Tobacco Control (FCTC) was adopted in 2003 with the purpose of setting international standards for tobacco control. Based on the WHO FCTC treaty, in particular Article 15, the member state parties created the Protocol to Eliminate Illicit Trade in Tobacco Products (the Protocol) as a separate international treaty with the objective of eliminating all forms of illicit trade in tobacco products through a package of measures to be taken by countries acting in cooperation with each other. The Protocol was developed in response to growing international trade in illicit tobacco products and the threat it poses to public health, loss of revenue to governments, and funding of international organized crime and terrorism.

The Protocol came into force on 25 September 2018 and the first meeting of the parties (MOP1) took place in Geneva between the 8th and 10th of October 2018. MOP2 will take place in the Netherlands in November 2020.

To date, the Protocol has been ratified by 57 parties. It presents a comprehensive set of tools to fight illicit trade of tobacco products, among them, the establishment of a tracking and tracing system, as well as measures to promote international cooperation, including sanctions, law enforcement, and other measures.

It focuses on securing the supply chain of tobacco products, which are defined as "products entirely or partly made of the leaf tobacco as raw material, which are manufactured to be used for smoking, sucking, chewing or snuffing."

II.   New OECD Guidance on transparency of Free Trade Zones and its Code of Conduct which came out last month[13]

The OECD Council has adopted the Recommendation on Countering Illicit Trade: Enhancing Transparency in Free Trade Zones.

The Recommendation on Countering Illicit Trade: Enhancing Transparency in Free Trade Zones was adopted by the OECD Council on 21 October 2019 on the proposal of the Public Governance Committee. The Recommendation aims to assist governments and policy makers in reducing and deterring illicit trade conducted through and inside Free Trade Zones (FTZs).

---

[12] https://www.who.int/fctc/protocol/illicit_trade/protocol-publication/en/
[13] https://legalinstruments.oecd.org/en/instruments/OECD-LEGAL-0454

Over the past decades, FTZs have been established at a record rate to attract new business and foreign investment. Their aim is to facilitate trade and economic growth by eliminating tariffs, quotas, and other taxes and minimising bureaucratic requirements, including certain customs procedures and disclosure requirements. While FTZs produce economic benefits to their local economies, there is strong evidence that illicit trade (e.g., counterfeits, wildlife, arms, etc.) flows through them. OECD analysis has identified a positive correlation between the size of FTZs – in terms of employment and numbers of firms – and the value of illicit trade in counterfeits. Some FTZs are also found to be key trans-shipment points for illicit goods that have been repackaged or re-labelled to conceal their point of origin, before entering the legitimate supply chain.

Development of the Recommendation: The 2017 Ministerial Council Statement recognised the need for international cooperation and partnerships to fight international corruption and illicit trade. Subsequently, the OECD High Level Risk Forum agreed in December 2017 that its Task Force on Countering Illicit Trade should develop a draft set of guidance on countering illicit trade. Building on several years of previous analytical work and expert consultation, an initial draft was discussed in March 2018, which included written inputs from consultations with the Financial Action Task Force, the World Custom Organization, and the World Trade Organization Secretariats. As a next step, an on-line public consultation took place from July to September 2018. A variety of stakeholders provided input, including representatives from OECD Members and non-Members, FTZ operators, their associations, intermediaries (including shippers, freight forwarders, and couriers), and industries established in FTZs or using FTZs in the course of their supply chains. Over 200 individual stakeholders participated, with nearly 100 pages of written comments received.

Scope of the Recommendation: The Recommendation is designed to ensure transparency in FTZs and is framed as part of the broader effort to counter illicit trade. It calls on Adherents to encourage FTZs to adopt a voluntary Code of Conduct for Clean Free Trade Zones that is set out in the Appendix to the Recommendation. Compliance with all the provisions of the Code of Conduct will be assessed and monitored by a mechanism (diagnostic tool) to be established within one year after the adoption of the Recommendation.[14]

III.   Panama Resolution[15]

The Colon Free Zone (CFZ) in Panama adopted measures to reduce illicit tobacco trade in line with international standards.

The CFZ, located near the Atlantic entrance to the Panama Canal thru the Caribbean Sea in Panama, has become one of the largest FTZs in the world. Due to its unique geographic location, more than 2,600 companies established in the CFZ are engaged in the import, sale, and re-export of different type of products, including sensitive commodities such as alcohol, cigarettes, and pharmaceutical products.

The CFZ has become one of the largest distribution centres for illegal cigarettes across Latin America. Therefore, there was a need to promote and advocate for a more stringent regulation at the CFZ in Panama, to ensure transparency in trade and to prevent the misuse of the zone by criminal organisations, while at the same time avoiding harming the broader legitimate business activities that drive economic growth.

On 25 April 2019, Panama published Resolution No. 8/2019 introducing measures to ensure trade facilitation, transparency, and the exchange of information between the CFZ Administration, the companies operating in the CFZ, and other government entities (the Resolution).

---

[14] https://legalinstruments.oecd.org/en/instruments/OECD-LEGAL-0454
[15] https://www.gacetaoficial.gob.pa/pdfTemp/28761/72527.pdf

The Resolution signifies a key regulatory milestone, with aspects of it representing global best practices. In light of Article 12 of the Protocol which specifically relates to FTZs, governments can look to Panama for inspiration on how to establish a framework to implement the provisions. While Panamanian authorities must still implement and enforce the provisions of the Resolution, its publication marks a significant step in combatting illicit trade in the CFZ. In that sense, the Colon Free Trade Zone Administration promoted the creation of the new Technical Committee to advise this administration on issues such as: illicit trade prevention, crime control, enforcement of existing regulation, etc., and obviously the further technical implementation of the Resolution No. 8/2019. This Committee gathers members of the UK Embassy, U.S. Embassy, Netherlands Embassy, PNUD, Spanish Cooperation Department, Customs and Border Protection U.S. Embassy, Inter-American Development Bank, International Organization for Migration, and University of Panama. It also counts the active participation of CSI Panama.

IV.   The US CITTPA (Combatting the Illicit Trade in Tobacco Products Act)[16]

In the U.S., several members of the House of Representatives have introduced the Combating the Illicit Trade in Tobacco Products Act (CITTPA). A similar legislation has been introduced in the Senate.[17]

The CITTPA would improve the U.S. Government's ability to identify and deter those engaging in the trade of illicit tobacco. Specifically, the CITTPA would:

- **Enable the U.S. to deter countries involved in the illicit trade in tobacco, and better assist its allies.** The bill grants the U.S. Secretary of State the ability to withhold U.S. foreign assistance from those countries knowingly profiting from the illicit trade in tobacco or its activities. In countries where the government is working to stop these trafficking efforts, the Secretary of State would be able to provide assistance for law enforcement training and investigative capacity.
- **Help the U.S. target individuals assisting in the illicit tobacco trade.** It authorises the U.S. President to impose economic sanctions and travel restrictions on any foreign individual found to be engaged in the illicit tobacco trade and requires the President to submit a list of those individuals to Congress.
- **Provide better information on countries involved with the illicit tobacco trade.** The legislation requires the U.S. Secretary of State to report annually on which countries are determined to be a major source of illicit tobacco products or their components and identify which foreign governments are actively engaged in and knowingly profiting from this illicit trade.

Co-sponsors of the CITTPA in both the House and Senate have explained why this legislation is so critical to combatting illicit trade in tobacco:

- "The illicit tobacco trade supports political corruption, organised crime, and terrorism worldwide. Our bill would take aim at this source of financing from these bad actors and the governments that enable them," said Helsinki Co-Chairman Senator Roger Wicker (R-MS).
- "The illicit trade in tobacco underpins some of the gravest transnational threats to the United States and our allies. Illicit tobacco trafficking is not a victimless offense; it facilitates other, more heinous crimes including money laundering and trafficking in weapons, drugs, antiquities, diamonds, counterfeit goods, and—worst of all—human beings," said Representative Sheila Jackson Lee (D-TX).
- "Cigarette smuggling is not just an economic issue, it's a public safety issue. Illegal cigarettes help finance organised crime and terrorism. Smuggled cigarettes are also more likely to end up in the hands of children and teens. The Combatting the Illicit Trade in Tobacco Products Act will give the United States better tools and more information to combat this dangerous activity," said Representative Richard Hudson (R-NC).

---

[16] https://www.congress.gov/bill/116th-congress/house-bill/1642/text
[17] https://www.congress.gov/bill/116th-congress/senate-bill/1965/text

Recommendations

Illicit tobacco trade is a complex, global, and growing problem that can only be solved if industry, governments, law enforcement, and civil society work together. Our significant experience, sincere commitment, and global understanding are offered to the Committee by way of the observations and recommendations made in this submission. No one organisation or institution can eradicate the illicit tobacco trade alone as it requires effective policies, continued focus, and coordinated actions by all.

There are several recommendations below on how to combat illicit trade through addressing aspects that drive both the supply and demand of illicit tobacco. For the purposes of alignment, there are some recommendations carried across from our earlier submission (Attachment A).

I.   Develop and implement a National Illegal Tobacco Strategy

A National Illicit Tobacco Strategy would provide a clear roadmap for all governments (federal and state/territory), agencies, industry, and retailers to focus and coordinate actions, cooperation, education, and direction.

As outlined above, there have been some significant and welcome reforms by the Federal Government over the last few years; however, one of the biggest challenges we now faced is in relation to aggressively enforcing existing laws that prohibit the retail selling of illicit tobacco.

Agreement and harmonisation of a strategy would provide clarity on roles and responsibilities in relation to enforcement and penalties applicable to those found breaking the law. It could also be used by states and territories to develop and share best practices that can easily be applied in all states and territories.

II.   Agree on the scale of the problem: measure and monitor

The first step in tackling illicit trade is to develop an understanding of the scope of the problem, its origin, and what is driving supply and demand. Reliable research methodologies exist to accomplish this; however, they have not been applied consistently or globally and remain controversial in Australia despite adoption by responsible law enforcement authorities in Europe and elsewhere around the world. By taking a more comprehensive approach to collecting data about the illegal tobacco market we will improve understanding of trends, product types, volumes, sources, and destinations.

This research methodology is required to understand the size of the problem and, more importantly, to track trends over time. This means that the work of measuring and monitoring is ongoing. Criminal gangs involved in smuggling are quick to respond to enforcement efforts. They change production centres, smuggling routes, and distribution networks in next to no time. For this reason, thorough, comprehensive, and regular monitoring to identify and anticipate changing trends and patterns is essential.

Developing a robust approach to measure illicit trade should include improving the tobacco industry methodology and sharing learnings and available data for ABF and Australian Taxation Office efforts to develop a measure system for illicit trade.

In addition to measuring the total volume of illicit trade, it is also important to obtain information on trends, types of illicit tobacco, source countries, usage demographics, and sales channels.

III.   Public & Private sector cooperation

Policy should be complemented by cooperation agreements between law enforcement, the legal tobacco industry, and others who have a role to play in tackling this problem.

Coordination, resources and time

Stamping out illicit trade requires coordinated and committed action by the public and private sectors on a continuous basis. Local and international cooperation involving governments, enforcement agencies, manufacturers, retailers, and consumers is critical.

We cooperate closely with government and law enforcement agencies and provide support to authorities' efforts to find, track down, confiscate, and destroy illicit tobacco products.

Information sharing is an important aspect of this cooperation. For example, we share intelligence gathered through the several research projects and investigative operations we conduct across the globe every year with the authorities.

PMI has signed many cooperation agreements with national governments and individual law enforcement agencies around the world. As of 2018, PMI has Memorandums of Understanding with customs and governments in 49 countries as part of concerted efforts to act against illicit trade[18]. In 2018, we provided anti-illicit trade awareness and PMI forensics technical training to 900 recipients during 41 sessions in 14 countries helping them to understand illicit trade issues and consequences, and technical knowledge on PMI product authentication.

In order to ensure that effective supply chain controls are in place and to determine points where goods might be diverted from normal sales channels, we respectfully request the ability to inspect and collect codes from PMI products before destruction.

Intelligence

The tobacco industry has developed significant resources to address the illicit trade in tobacco products, constantly investing to develop a better understanding of the market, its drivers and enablers, current volumes and trends, and the way the criminals behind it work.

The intelligence we gather locally in Australia and around the globe through numerous initiatives is available to be shared with law enforcement and other authorities to support efforts to fight illicit trade. Feedback also helps the industry to enhance our controls and strategies to further secure our supply chain.

IV.   Effective Policy to regulate the supply chain

Regulation of the legal tobacco market should assist in identifying when products are being manufactured, sold, or distributed outside of the legitimate supply chain. The following regulatory measures should be part of the tobacco policy framework to combat illicit trade and apply equally to all participants regardless of the size of their business:

- **"Know your customer"**: Legal tobacco manufacturers, wholesalers, distributors, and transporters should be required to conduct due diligence with respect to their customers. This due diligence should include:
    o Verification of a customer's legal right to trade in or purchase tobacco products;
    o An assessment of whether the volumes being purchased are consistent with the customer's demand or sales;
    o A process for reporting suspicious transactions; and

---

[18] https://www.pmi.com/resources/docs/default-source/sustainability-reports-and-publications/pmi-sustainability-report-2018-low-res-may-2019.pdf?sfvrsn=47ef95b5_4

- o A policy enabling business relationships to be reviewed and terminated when laws have been broken.

- **Tracking and tracing**: Tracking is the ability to monitor finished goods as they make their way through the supply chain from the point of manufacture. Tracing is the ability to recreate the movement of goods up to a certain point in the supply chain to help determine if the product was diverted into illegal channels at some point in the process. Tracking and tracing help to combat the diversion of genuine products. We acknowledge recent amendments to the Plain Packaging Act to allow for coding to be printed on packs and cartons, however the amendments require certain colours to be used which makes the codes unreadable by machines and, therefore, redundant for large-scale tracking and tracing.

- **Record keeping**: The legal tobacco supply chain should be required to maintain complete and accurate records of all relevant transactions for five years and to make records available to relevant law enforcement authorities.

- **Licensing**: Combined with strong enforcement and deterrent penalties, a licensing or equivalent approval system that ensures only legitimate and law-abiding businesses can engage in the manufacture, import, and export of tobacco products, manufacturing equipment and key components of cigarette manufacturing, especially cigarette paper and filters. While few of these 'upstream' elements of the tobacco industry exist in Australia, the supply of cigarette tubes, papers, and filters are essential to the functioning of the illicit "chop chop" market and should be licenced at the import level and monitored at the retail level.

- **Enforcement in FTZs**: These tax-free locations were originally developed to enhance global trade and the free flow of goods. Recently however, they have become a preferred place of doing business for smugglers and illicit white cigarette manufacturers. Therefore, the measures highlighted above should be implemented and enforced in these zones. Many seizures by the ABF have been linked to tobacco products produced in or transported through FTZs. The International Chamber of Commerce's Business Action to Stop Counterfeiting and Piracy (BASCAP) report, *Controlling the Zone: Balancing facilitation and control to combat illicit trade in the world's Free Trade Zones*[19], provides useful recommendations in relation to this issue.

- **Control of key components:** Cigarettes are made of three main components: tobacco, paper, and filter. Without any of these components, cigarettes, legal or illegal, can't be produced. Implementing strict controls over the production and supply of each of these key components can therefore be one way to make the production of illegal cigarettes more difficult for criminals.

Intermediaries involved in the supply chain should also be regulated to eliminate global supply chain vulnerabilities.

V.   Technology

Technology plays a central role in the effective control of legal supply chains and in the fight against illicit trade. We implement cutting-edge technological solutions in areas such as product authentication and tracking and tracing that have become the industry standard. In the past, in line with what governments were expecting from manufacturers at the time, we focused our efforts on controlling the sales of our products to our direct customers.

Over the many years that followed, governments' views and expectations from manufacturers changed, requiring that we oversee the flow of our products even when they are out of our direct control. We have kept pace and continued to expand our controls further down the supply chain.

---

[19] *Controlling the Zone: Balancing facilitation and control to combat illicit trade in the world's Free Trade Zones*, BASCAP, 2013: https://iccwbo.org/content/uploads/sites/3/2016/11/Combating-illicit-trade-in-FTZs-1.pdf

Over time, we developed a deeper understanding of the unique nature of the illicit tobacco trade and implemented a broad range of measures and technologies that are recognised today as effective solutions to further prevent the diversion of our products from the legal supply chain.

There are many technologies that claim to prevent illicit trade but in reality, none will stop copies being made, or cigarettes being smuggled, or illicit whites. However, some technologies can give governments, retailers, and consumers the ability to rapidly determine whether duty has been collected on a product, as well as if the product is genuine or fake.

Specifically, these technologies can improve the security of the supply chain in three primary ways:

1. **Tracking and tracing** can help address smuggling of tobacco products across borders.
   o **Tracking** is the ability to monitor finished goods as they make their way down the supply chain from the point of manufacture.
   o **Tracing** is the ability to recreate the movement of packaged tobacco products back up the supply chain to a certain point.
   o A track-and-trace regime can contribute to preventing the diversion of tobacco products into illegal channels.

2. **Authentication** can help address counterfeiting.
   o **Authentication** is the ability to determine genuine products from counterfeit.
   o One of the most secure authentication solutions used today by various industries is to print a unique code on each and every pack. This code can then be scanned (e.g., with a smart phone) by consumers, retailers, and law enforcement officials to determine whether that pack is genuine.

3. **Digital Tax Verification** can help to address tax evasion.
   • **Tax verification** involves verifying that the declared volume of tobacco products manufactured matches the amount of excise tax due and paid.
   • Digital fiscal marking of tobacco product packaging is used in many countries around the world as a tool to verify the payment or collect tobacco taxes. Codes that are directly printed on, or attached to the pack, are very common ways of doing this. The markers are used by auditors to ensure the number of codes or stamps used by the manufacturer match the number of tobacco products sold, in stock, or rejected during the production process.

All these technologies can contribute significantly to tackling illicit trade and should be considered as part of a comprehensive strategy.

VI.   Awareness and Education

There is a lack of awareness about the reality of the illicit tobacco trade that can only be resolved though educating the public. As such, raising public awareness about illicit trade and its consequences is key to tackling the demand for illegal tobacco. PMI promotes awareness campaigns in several countries that are designed to inform the public and raise governments' attention to the negative consequences of illicit trade. We also educate retailers about the serious implications of selling illegal cigarettes and offer advice on how to avoid becoming involved in the illicit trade.

One of the most effective ways of reducing illicit trade is to help consumers identify the difference between legal and illegal products and the risks involved in purchasing illegal tobacco. Unfortunately, low public awareness and understanding of the issue means that many smokers buy cheap, illegal cigarettes with little knowledge of where the product comes from, what it contains, or the extent to which their money is contributing to fund organised criminal activity.

Public information campaigns are essential

Informing consumers about the societal and financial impact of the illegal cigarette trade, as well as publicising seizures made by enforcement authorities and prosecutions must be a core component of any plan to tackle the illicit tobacco trade. A 2009 report conducted by BASCAP observed:

> *"Only when consumers appreciate the full repercussions of their counterfeit purchase can they be expected to stop the practice."*

Numerous parties, including government agencies, tobacco manufacturers, media outlets, cross-industry groups and associations, and legal retailers, can and should play an important role in developing education campaigns. Broad use of local and national media to raise public awareness of these campaigns is also critical and is an approach effectively adopted by the European Anti-Fraud Office.