

**Commission on Security & Cooperation in Europe:
U.S. Helsinki Commission**

“A Hazy Crisis: Illicit Cigarette Smuggling in the OSCE Region”

Committee Members Present:

**Senator Roger Wicker (R-MS), Chairman;
Senator John Boozman (R-AR)**

Witnesses:

**Louise Shelley, Director, Terrorism, Transnational Crime, and Corruption
Center, George Mason University;**

**David Sweanor, Adjunct Professor of Law, University of Ottawa;
Marc Firestone, Senior Vice President and General Counsel, Phillip Morris
International**

**The Hearing Was Held From 9:30 a.m. To 10:38 a.m. in Room 106, Dirksen
Senate Office Building, Washington, D.C., Senator Roger Wicker (R-MS),
Chairman, Commission for Security and Cooperation in Europe, presiding**

Date: Wednesday, July 19, 2017

WICKER: This hearing of the Helsinki Commission will come to order. Welcome, and good morning to everyone.

The Commission is mandated to monitor the compliance of participating states with the consensus-based commitments of the OSCE. Today's hearing of the Commission focuses on the multidimensional issue of illicit cigarette smuggling in the OSCE region.

Illicit cigarette smuggling is a significant transnational threat. I would say again it is a significant threat: ongoing illicit trade helps fund terrorist activities, it fosters corruption, and it undermines the rule of law.

European Commission and KPMG studies estimate that around \$11.64 billion is lost every year to this criminal activity in the European Union alone, where counterfeit cigarettes are particularly prevalent and account for nearly 30 percent of the articles detained by EU customs.

This issue involves two of the three dimensions of the Helsinki Final Act, the first being hard security and the second being economic issues.

Illicit cigarette smuggling's link to hard security is evident in a recent report issued by the Department of State in conjunction with the Departments of Treasury, Homeland Security, Health and Human Services, and Justice. The report emphasizes what I have already said in this opening statement, and I quote: "Illicit tobacco provides a significant revenue stream to illicit actors," unquote, and, quote, "fuels transnational crime, corruption and terrorism." So, for these reasons, it's important that we be here today. And the report declared that the global illicit trade in tobacco poses a threat to national security.

Building upon former commitments, the OSCE established a Charter on Preventing and Combating Terrorism in the aftermath of the September 11, 2001 attacks in New York and Washington. That charter targeted four strategic areas for specific action: policing, border control, trafficking, and money laundering. I hope today's witnesses will consider how measures taken pursuant to that charter are being applied to the illicit trade in tobacco and tobacco products.

With regard to economic issues, illicit trafficking in cigarettes is a major source of corruption. International criminal organizations that engage in tobacco trafficking generate profits that are then available to corrupt public officials and subvert the rule of law. The Department of State estimates that the worldwide tax loss from illicit tobacco smuggling is between 40 billion (dollars) and \$50 billion annually. This is money that is lost to taxpayers, further weakening state institutions while enriching and empowering criminal elements that are themselves a threat to those institutions. These are serious challenges in many emerging-market economies within the OSCE, and I hope we will hear more today from our witnesses about the scope of the threat and the measures that can be taken to combat it.

Underlying all of these problems is the fact that there is enormous money to be made in illicit tobacco trafficking. An OECD report issued last year concluded that cigarettes present high profit margins, and are among the most commonly traded products on the black market due

to the relative ease of production and movement along with low detection rates and penalties. The OECD cited many reasons for the growth of the illicit trade in tobacco. Today we will engage in an in-depth examination of those reasons and identify potential responses.

To help us do that, we have three very distinguished witnesses.

Dr. Louise Shelley is a professor and the director of the Terrorism, Transnational Crime, and Corruption School of Public Policy at George Mason University. She is a leading expert on the relationships among terrorism, organized crime, and corruption, and she also specializes in illicit financial flows and money laundering. I assume you specialize in the study of – (laughter) – money laundering. Dr. Shelley serves on the Global Agenda Council on Illicit Trade of the World Economic Forum, and she was the first co-chair of its Council on Organized Crime. Dr. Shelley has frequently testified on Capitol Hill regarding issues that impact national security.

Professor David Sweanor is an adjunct professor of law at the University of Ottawa. Professor Sweanor has pioneered efforts to reduce cigarette smoking in Canada and around the world. As part of those efforts, he has worked with groups such as the World Health Organization, World Bank, and the Pan American Health Organization, the latter of which honored him with the Public Health Hero Lifetime Achievement Award. Professor Sweanor has previously testified before the Canadian Parliament and the U.S. House, and is back before the – and the Senate, and is before the Helsinki Commission for the first time.

Mr. Marc Firestone is the senior vice president and general counsel for Phillip Morris International. In that capacity, he helps guide the company's global response to the illicit trade in tobacco.

We hope to accomplish three things at today's hearing. First, we hope to draw attention to the problem of illicit tobacco trafficking – how it helps fund terrorist activities, foster corruption, and undermine the rule of law – have I said that enough times? – and why the United States should provide leadership in this fight. Second, we hope to learn more about best practices in both the public and private sectors to minimize illicit tobacco trafficking, and deny the financial proceeds of such trafficking to terrorist and criminal groups. Third, we hope to increase an understanding of how illicit tobacco undermines public health policy.

So thank you to these distinguished members of today's expert panel for joining us today, and I look forward to our discussion. Perhaps we can begin with testimony by Dr. Shelley.

SHELLEY: Thank you for this great honor, and it's a great pleasure to speak again before the Helsinki Commission. One of my first congressional testimonies was on the issue of human trafficking before this Commission, and with Congressman Smith's support.

I've been following this issue of cigarette smuggling and illicit trade for a long time, and it has taken me to many different locales. More than a dozen years ago I was in Georgia, where our research had shown that there were linkages between the illicit cigarette trade and Iraq. And when I talked about this in a public meeting, it was one of the first times in my research career in

which I was threatened. So it tells us that illicit cigarette trade is not a benign activity, and traffickers will even go after researchers.

More recently, I have visited the open markets in Paris where cigarettes are sold en masse, and France is the contraband capital of Europe for illicit cigarette trade. And it's hardly surprising that one of the Kouachi brothers, who murdered the journalists of Charlie Hebdo, received some of his income from the illicit cigarette trade.

Also, I have visited the markets of illicit cigarettes in Italy, which are very much under the control of organized crime. So we see very different variations in this problem, but many, many elements of it across the OSCE region.

I've also spoken to investigators in New York who work closely with their international counterparts, as there is an important crime-terror connection to illicit cigarette trafficking in the United States.

What is important, I think, to point out, beyond your opening and very clear remarks, is that there has been a problem of a culture of impunity. As I have in my longer written statement, the former president of Montenegro won the award from the Organized Crime and Corruption Reporting Project as criminal of the year one year ago because of his very important role in the illicit cigarette trade. So it's not just criminals, it's not just terrorists, but it's high-level officials that are not just in policing or in the borders but at the heads of national governments, that are involved in this.

Beyond this, we need to look at the importance of hubs outside the OSCE region and what they're doing in facilitating the trade of the illicit cigarettes that move into Europe and also into North America. Free-trade zones like the Jebel Ali Free Zone in Dubai is absolutely central to this.

Furthermore, we need to be thinking about illicit cigarette trade as not a standalone crime. It converges with the drug trade, with wildlife smuggling, trade in counterfeit goods, and other crimes. Illustrative of this is a case that occurred in the Czech Republic in which the Czech police that were monitoring illicit cigarette trade tipped off members of the customs police in the Czech Republic to the fact that a shipment of rhino horn was about to be arriving in the Czech Republic from South Africa. What this tells us is that there is a convergence of different crimes, and also that the cigarette trade often serves as what I call venture capital for other forms of serious crime, so that the money that you get from this petty trade that you can start with leads you to even higher revenue streams that can have very corrosive impact.

Also, we need to be thinking about the role of companies in facilitating this trade. In my written statement, I cite a problem that British American Tobacco cited and Imperial Tobacco with Facebook in the U.K. where posts on Facebook were facilitating the delivery of cigarettes in that country, and the same thing has been found by PMI in France. And yet, there has been very limited response from the new media companies that are facilitators of this trade. And just as we've put pressure on the new media to be countering terrorist recruitment, we also need to be focusing on how they are facilitating illicit trade.

Part of the reason that this is going on is that there is an absence of a law enforcement response. And my last book, which was called “Dirty Entanglements: Corruption, Crime and Terrorism,” I had a whole chapter on the funding of terrorism through what I called underpoliced crime. And cigarette trade figured in that chapter because of the absence of resources and the absence of an adequate law enforcement response.

So the prevalence of illicit cigarette trade reveals the limits of our strategies to counter illicit trade. In my statement, I’ve provided some text from my forthcoming book that I’m just completing on illicit trade. And in it, I show how there is a merger of problems that we’re facing, especially in Europe today and in our community of the OSCE, with the illicit cigarette trade.

And I start off with a case of going to the Museum of Immigration in Paris and listening on a – on a broadcast on earphones to a migrant describing his problems in Europe. And he describes how he arrived illegally in Italy and can’t find employment. He traverses Italy. He goes to France and, finally, winds up in Marseille, and says: “In Marseille, I’m now working – I’m working as a cigarette seller.” But what it doesn’t say is that he’s working in the illicit cigarette markets, where 40 percent of the sales of cigarettes in Marseille, a hub that also connects with terrorism, are illicit cigarettes. And so, as Europe fails to integrate its masses of illegal migrants, it is also fomenting the problem of illicit trade because illicit activities cluster where individuals who cannot work legitimately work in illicit markets.

So what do we need to do to address this problem? First of all, we need to allocate more law enforcement responses to this, and to do the kind of network analysis, analysis of hybrids, following the money that is not done enough in relationship to this crime. We need to address not just the low-level corruption, but the high-level corruption that facilitates this trade.

About 10 days ago, when I was talking about this in front of the security assembly of the Annual Security Review of the OSCE in Vienna, I talked about these problems of new trends which we’re looking at. And subsequently, I went to a rollout of a publication called the “Crooked Kaleidoscope – Organized Crime in the Balkans,” which made the same point as I do – and I’ve cited it in my report – that high-level corruption is behind this trade in the Balkans.

We need to require corporations in the new media space to focus more on their facilitating role, and that needs to be part of a larger effort to focus on public-private partnerships.

And we need to pay more attention to the facilitating role of free-trade zones in illicit trade.

And as a researcher, I suggest that we need to focus much more on understanding the illicit flows, the hubs of the trade, and the convergence of different forms of illicit trade, because insights from one kind of criminal activity can help in fighting another.

We need to work on the harmonization of tax policies on cigarettes because it is the discrepancies in pricing that provide so many of the financial incentives for participation.

And we need to provide serious analysis of the optimum tax rates on cigarettes that address state revenue concerns, but also do not contribute to smuggling. About 10 days ago, I was in France and listening to the radio, and it said they need to increase their taxes on cigarettes in France to reach 10 euros a pack. But there's no analysis of what this will do to illicit markets, though the radio commented that they imagine that this would increase the problem, where already France is number one in Europe.

So we need to do serious policy analysis that will help us address this issue. It is not just a small-scale problem. And as you mentioned in the introduction, it is very crucial to state revenues, state capacity, and to national security.

Thank you.

WICKER: Well, thank you very much.

And Mr. Sweanor, you are recognized next. Thank you.

SWEANOR: Thank you, Mr. Chairman. It's a pleasure to be here despite the weather in Washington in July.

I've worked as a lawyer on public health issues around tobacco and nicotine for over a third of a century, and a lot of that time has been spent dealing with issues of tobacco taxation and then with the contraband trade – monitoring it, trying to understand it, litigating on it in order to try to deal with the problem. I think there are a few basic facts to start with.

To date, price is by far and away the most powerful tool that's been used globally in reducing cigarette smoking. I mean, it just completely dwarfs what we've accomplished with our other measures. So it is a very, very powerful tool. But beyond the elasticity of this – there's the cross elasticity, as economists would say – people will move between product categories based on differences in price, whether it be between different tobacco products or, in this case, between licit and illicit products. That's just a reality of the market, and it's odd that a lot of people will deny that – either claim that price is the single factor dictating whether there's going to be a contraband trade or that price doesn't have any impact, tax doesn't have any impact, often depending on somebody's ideological or vested interest.

But I think the way to see this is simply as a business. People get involved in the contraband trade in order to make money. And profitable smuggling really depends on pretty simple economics. It's a matter of what's the cost of acquisition of the goods, what's the cost of dealing with the goods, and what's the profit margin and the size of the market for selling those goods?

Cigarettes create a tremendous opportunity in many places, and few as much as what we see in Eastern Europe, where the cost of acquisition is very small. If you're manufacturing

cigarettes, you can usually do it for one or two cents per cigarette. There's areas in Central Europe I've been able to buy packages of cigarettes for 20 cents, and told by my interpreter that I was being ripped off because I was a North American. They've very inexpensive to make.

The cost of – as we've just heard from Dr. Shelley – the costs of being involved in the business, the chance of apprehension, the penalty should one get caught can be extraordinarily low. And the ability to sell those products to a largely lucrative market is pretty much unparalleled, because for Eastern Europe it's a short trip into the European Union. And, you know, as we've heard, the price of cigarettes can be very high.

So there's a particular problem there. And I think the solution, in large part, is dealing with the business viability. What can we do that creates a higher cost for acquisition? What can we do that increases the cost of dealing with the product? And what can we do that reduces the market for the illicit products? And that's a matter of things like how do we limit the availability of the manufacturing machinery, the supplies that are used in manufacturing cigarettes and the people who are engaged in that? And there's been various measures aimed at trying to do that sort of thing.

But also, dealing with the supply of cigarettes that are just sort of floating around the gray market. I mean, the – there has been a long history of a huge difference between the number of cigarettes legally exported and the number legally imported. And that's a key issue to go after. And I've been involved in that, with racketeering actions here in the States against multinational cigarette companies for products that were sort of disappearing and showing up in the European Union. And I think that was very successful, because it largely ended by trade by changing the economics. It greatly reduced the supply of cigarettes that were available.

We can do more, though, on increasing the cost to the business through things like enforcement, increasing chance of apprehension, track and trace technology that makes it easier to figure out where products came from, trace it back to the manufacturer. The penalties that we end up levying, making it easier for people to enforce actions, including U.S. law, in order to put up the cost for criminals being involved in this sort of business.

And then finally, and in an area that I think is neglected and shouldn't be, is what do we do about the demand for illicit trade? And I think that's worth expanding on, because it's – as I say, it's been oddly ignored that unlike most areas of illicit trade, the vast majority of people who are currently smoking cigarettes are telling us they wished they didn't smoke. You know, they're not smoking because they want to. They're smoking through some combination of dependence, addiction, self-medication.

But mainly, they're smoking because they're not given a viable alternative. And so they're buying – if the only alternative is legal cigarettes and illicit cigarettes, illicit cigarettes are way cheaper and widely available. But the challenge that we have, or the ability to address this I think is huge, and we're not paying attention to it. That what kills people from smoking is the smoke. It isn't the tobacco. It isn't the nicotine. It's the smoke. Cigarettes are an incredibly deadly delivery system.

If we met the needs by working with consumers to give them better access to alternative products, non-combustion products – the vaping products, the heat not burn products, the smokeless tobacco products, the pharmaceutical products – we could probably eliminate much of the demand for illicit trade by giving people a viable option that not only makes much better economic sense to them – because it can be cheaper, because so much of the price of cigarettes is tax – so it can be cheaper, but it also can save their lives rather than kill them.

That's a huge possibility. If we made those products available, if we allowed people to get accurate information about those products, we get to change the market. You know, just like we can eliminate the market for fake – snake oil medicines by having licensed pharmaceutical products, we could change the market by having products that are far harder for people to counterfeit and consumers are far less likely to want to buy, because we're giving them a viable alternative to cigarettes.

So I think that that, going after the end consumer, working with consumers, would be incredibly important. And we have the ability to use policy tools. I co-authored an article in the New England Journal of Medicine a couple of years ago, and using differential taxes for products with differential risks – we could be using those types of measures around the world. There's no reason to tax the low-risk products. We can affect the differentials in marketing, product standards, product placement. Give the people who are buying illicit products a viable alternative to them.

But in looking at particular measures, I think that the use of existing laws, including here in the United States with the racketeering laws, RICO laws, which as I said I've been involved with before, to battle the criminal gangs, make it easier for the states that are – that are losing such huge sums of money to criminal gangs to use U.S. courts as one of their avenues for going after the criminal gangs.

It's very hard for anybody to be involved in widescale money laundering without using U.S. banks. That brings them within the purview of U.S. law. Get rid of things like the Common Law Revenue Rule that was making it hard for any government to collect forgone taxes using the U.S. courts. Help them go after these criminal gangs. Make it possible to take the money away from these gangs, and they'll stop doing what they're doing because you've destroyed the business viability.

I – again, non-combustion alternatives. Give people alternatives to the sorts of illicit products that they're buying now. Recognize that the whole tobacco-free world approach that's been taken by U.S. government agencies has unintended consequences. And the unintended consequences include that if you don't give people alternatives to cigarettes as a product, the alternative they're going to find is illicit cigarettes. We have the ability to make real changes in those things. And I think it takes some vision. It takes some creativity. But the options are available and we can do meaningful things to deal in a serious way with a tremendous problem that's affecting health, it's affecting revenue, and it's promoting criminality. Thank you.

WICKER: Thank you very much.

Mr. Firestone, you're recognized.

FIRESTONE: Yes, sir. Thank you, Mr. Chairman. Thank you very much for holding today's hearing on the illicit tobacco trade. As you've said, and as Professor Sweanor and Professor Shelley have said, it is indeed a significant problem. And it's one that merits, undeniably, this Commission's expertise, attention, and authority.

In my role as general counsel at Philip Morris International, PMI, I'm ultimately accountable for the company's compliance programs and our anti-illicit trade efforts. And it's, indeed, an honor for me to appear before you today on this topic. PMI is the world's leading tobacco company. We employ 82,000 people around the world. We do not sell products in the United States, but we're among the largest buyers of American-grown leaf tobacco, and proud to support the livelihoods of farmers in this country.

The battle against illicit tobacco products concerns both the private and the public sectors. And we welcome this hearing as further evidence of the determination of the United States government to confront a major social issue. Cigarette smuggling exists on a large scale around the world. For criminal organizations, there are huge profits. For governments, there are huge losses. As you've said, estimated at over \$40 billion per year. For PMI, we welcome competition, and we compete aggressively for market share, while playing by the rules.

But gangs that sell smuggled cigarettes have an illegal price advantage versus legitimate companies. They're not competing based on product quality or other benefits to consumers. Their success comes from rank cheating. Their conduct corrodes lawful markets, and robs treasuries around the world of billions in tax revenues. Here's an example: Often criminals have their own brands of cigarettes – not counterfeit, but not legitimate either. And what they do is, in country A they make these brands solely to sell in the illicit channels in country B. And like termites, these illicit brands undermine country B's regulatory framework for tobacco products. Termite brands are a form of invasive species, and they make it easier for kids to buy cigarettes. They are out of compliance with health warning requirements. And they are on sale for illegally low prices.

But smuggling does more than destroy legitimate markets. It generates funding for other illicit enterprises, as Professor Shelley has said and written, from dangerous drugs to the true abomination of human trafficking. So this is not about tourists who occasionally take a few extra carton(s) of cigarettes through the nothing to declare line at an airport. This is not about casual transgressions. It is about a dangerous, high-profit machine whose activities spread far and wide.

Now, even as a legal and ethical business, PMI faces much controversy. And we certainly don't want to be anywhere close to the illicit trade. We've worked hard and invested a huge amount of money to put tight controls on our supply chain and run our business with keen vigilance to the risks of product diversion. We've continually increased our effectiveness through advice from leading experts, and through cooperation with governments, including, for example, those in Canada, the United Kingdom and Italy, as well as cooperation with the European Union and European Commission.

We are determined to be innovative. We are determined to remain at the forefront of industry in controlling a supply chain. But even the best possible commercial practices cannot change a few basic facts. PMI doesn't make or enforce anti-smuggling laws. We don't police borders. We can't tell other companies what to do. So in our view, there has to be an integrated, cooperative, comprehensive approach. There has to be control of all elements of the supply chain. And this definitely includes raw materials to make cigarettes.

For example, if criminals can't get the cellulosic acetate that goes into all cigarette filters, and if they have no access to other raw materials, they can't make these termite brands. Now, the pharmaceutical industry has seen success in controlling drug precursors, such as pseudoephedrine. And I believe there are many lessons from that industry in the present context. We also need stronger legal deterrence, such as those that exist against trafficking in narcotics, wildlife, and blood diamonds.

Legislation on tobacco and the fight against illicit trade should include provisions for identifying the worst offenders, for freezing their assets, and for imposing far stiffer penalties than often exist under current law. Our views rest on empirical evidence. Experience in a number of countries has shown that aggressive, well-funded enforcement, combined with the right laws and sincere cooperation from business can, indeed, dramatically reduce illicit trade. So my written testimony includes more detail on our recommendations, but I hope these examples show what we have in mind.

Now, today's hearing focuses on the OSCE region. But we're actually talking about a worldwide problem. And progress requires cooperation among regions and nations. PMI supports transparent implementation of WHO's protocol to eliminate illicit trade in tobacco. We urge international organizations to welcome, rather than exclude, the views of all subject matter experts including manufacturers, retailers, farmers, law enforcement officials, and, of course, ministries of justice, finance and health. That's the core group to counter the criminality that troubles us all. And I believe the U.S. has a great opportunity to show, indeed to lead, the way.

Mr. Chairman, I, again, thank you for the privilege and honor to appear before this esteemed Commission. And on behalf of PMI, I pledge our full support to the Helsinki Commission and the United States government as a whole in crushing the illicit trade in tobacco. Thank you, sir.

WICKER: Thank you. And thank you all. Without objection, the written statements of all three witnesses will be added to the record of this hearing.

Dr. Shelley, I believe you stated that new media is facilitating this illicit activity, and that new media corporations should be held to account and more requirements placed on them. Could you elaborate on that suggestion?

SHELLEY: Certainly. One of the things that facilitates deliveries is that people post meet at this point, a delivery is going to be here on Facebook pages and other forms of communication. And I think it's very important that we not have criminal facilitation through media. This requires the construction of algorithms and other means that are being used now, as

there has been a focus on countering statements of radicalization. There have been efforts by new media companies now to invest in this area, which they hadn't before.

And I think that's what – when I talk about corporate involvement, is that they cannot have as laissez-faire approach towards things that are harmful to society, like messages that recruit for terrorism, messages that allow for illicit deliveries. And if there was more monitoring of this kind of activity, some of it might go into the dark web, but that is not as easy to access as a Facebook page.

WICKER: And who should do the monitoring?

SHELLEY: I believe that this is part of what we need in having what Mr. Firestone talked about as a private partnership, because it is incumbent on the new media companies to be responsible about what they're posting. We can't have law enforcement come and force them to take this off. There have been efforts made previously, I know, through corporate channels to approach Facebook to be more careful about this monitoring, in this climate before terrorist radicalization. And this was rebuffed. And I think that we need to understand that our media can be a – social media can be a force for good, but it also needs to do much more policing of itself. Just the way I talk about, in my book, how platforms are selling counterfeit goods without adequate surveillance.

WICKER: To be clear, are you advocating government – a government role in enforcement in this – in this area of the new media?

SHELLEY: I wouldn't call it government enforcement. I would call it public-private partnership, where the government sits down with the new media, just as it's done in the area of terrorism, in saying: We have this problem. And we need your help, your resources to help do this for the collective good. And that's –

WICKER: And what agency of the government should do this?

SHELLEY: I think it needs to be a combination. I think it would be in part Bureau Alcohol, Tobacco and Firearms. It would be Homeland Security. It might even be also FBI. It would need to be an intergovernmental working group, such as produced that counterterrorism – or, I should say – that report on cigarette smuggling and its relationship to terrorism that you cited, Chairman Wicker, in your opening remarks. That was a coalition of government officials working to counter this threat. And I think they need to sit down with the private sector, this working group, and point out the problems that exist.

WICKER: Mr. Sweanor and Mr. Firestone, comments on this topic from either of you.

SWEANOR: I think if we look at what happened with the European Union challenging the cigarette companies over facilitating a trade, their actions are allowing product to become available to the smugglers, and closing that, I think it raises the same question that could be thrown at those who are facilitating the trade through information. What's their role in this?

I think of a discussion with them and the possibility – I’m not an expert in U.S. law – in U.S. racketeering law, but I think it does at least raise a question of do they have some responsibility for those billions of dollars that are being lost in those countries? Might that be enough to give them a wake-up call to say, we maybe don’t want to be facilitating this. We’d just as soon not end up in court with someone trying to recoup that money. But they need to accept some level of responsibility for this, as does everybody else along the supply chain.

And I would say, and as we all do, for having engaged in policies that prevent smokers from having viable alternatives to cigarettes. You know, they’re moving to illicit trade because we’re not giving them a better option.

WICKER: And I’m going to get to that in a moment.

Mr. Firestone?

FIRESTONE: Yes, Senator, thank you. I think it’s a very interesting and important point. And I think that for me, three points that come out of it. One, is it’s an example of how many different threads there are to the illicit trade in tobacco. And I think that’s maybe one reason that this area gets less focus than it merits, because if you look at each of these individual threads, maybe you say, well, it’s a problem but it’s not my top three priorities. But when you put them all together, it is. And I think that the availability of ads and so on for illicit products on social media is one of the threads.

Second, as Dr. Shelley and Professor Sweanor have emphasized, I think it’s important to tell everyone on the legitimate side of the business that you can’t have, in Professor Shelley’s words, a laissez-faire attitude. No, maybe one company can’t control everything, but all of the companies have to be doing their best to shut down these trades.

And third, and in respect to your question about agencies of the federal government, I would be optimistic that any agency that contacts any responsible public company – that company would be very responsive simply to know that the United States government is aware of what’s happening, and that the United States government has a concern that that company or our company needs to address.

WICKER: Dr. Shelley, we’re here at the corner of Constitution and 1st in Washington, D.C. How far do I have to go to buy some illicit cigarettes here in town?

SHELLEY: You can go to your computer.

WICKER: OK.

SHELLEY: And you can order them online and have them delivered to you in a shipment that will arrive either by the Postal Service or by UPS or FedEx, that segment their shipments.

WICKER: So, that’s the cleanest, safest way for me to engage in this illegal activity.

SHELLEY: Yes.

WICKER: So what – I mean, I'm pretty technically challenged. What website do I go to? Come on.

SHELLEY: You –

WICKER: The cameras are rolling. (Laughter.)

SWEANOR: You're facilitating illegal activities. (Laughter.)

SHELLEY: That I'm not going to do. But you could go to many providers that you –

WICKER: So, what would I need to click on?

SHELLEY: You could look at –

WICKER: So, what if I put in untaxed cigarettes?

SHELLEY: That, I don't think would be – well, you know, you could try that. I would also put in, you know, cigarettes at low price, bargain cigarettes. And if you found you were media-taxed, then I would go off to – or send one of your assistants off to some local bar, convenience store that'll sell you some cigarettes under the table.

WICKER: OK, now – so I go to a convenience store. How far away is this convenience store?

SHELLEY: I'd say we could find you one within a mile of here.

WICKER: OK. And how –

SHELLEY: Not a – you know, a small place. Not – you know, not a large convenience store.

WICKER: OK, so the name-brand convenience stores that advertise, they're going to stay away from this? OK.

SHELLEY: Generally, yes.

WICKER: So I go into – and how – and so I want some cigarettes, how do they know I'm cool? How – (laughter) – if I walk in dressed like this, they're probably going to sell me the taxed –

SHELLEY: They'll probably sell you the taxed cigarettes. That's why I said send in one of your assistants who might be in blue jeans, because the same enterprise often sells, as I write about, both licit and illicit products.

WICKER: OK, so how much is a carton of cigarettes going to cost me if I'm buying the right way, if I pay the tax and buy it over the counter?

SHELLEY: Well, it depends if you buy it in D.C. If you buy it in Maryland, there'll be another price. If you buy in Virginia there'll be another price. And that's part of the problem.

WICKER: OK. But typically, and so maybe, Mr. Firestone, I'm not leaving this line of questioning, but how much am I going to pay in Washington D.C. for a carton of whatever's?

FIRESTONE: I can't say exactly because we don't sell products here, but I think if you assume that a pack may be \$4 and there are 10 – if there are 10 in a carton, maybe \$40, \$50 a carton, a legal product.

WICKER: So, Dr. Shelley, how much am I going to pay for illicit?

SHELLEY: Probably about half that.

WICKER: OK, and is – if I'm particular about my product and I don't want a termite brand, can I get a name brand by clicking on the right source and ordering it online?

SHELLEY: Sometimes you can get a name brand.

WICKER: OK.

SHELLEY: Sometimes you have packages that are produced with even – how do I say – with counterfeit packaging, with counterfeit stamps put on them. There's a whole supporting industry that goes with this to falsify products. And there's also a problem of diversion. So we've had terrorist cases in the United States of funding for terrorism done by diverted cigarettes, where cigarettes have been taken from low-income states, low-taxation states like North Carolina, and shipped to New York or Michigan that have much higher tax rates. So then you would get a real cigarette that's been diverted from a market in another state.

WICKER: And I do this illegal thing, they ship it to my condo in Maryland – which I don't have a condo in Maryland – (laughter) – but what is my penalty and who's going to catch me?

SHELLEY: There's very little chance that you're going to be caught. The Postal Service is so busy monitoring shipments of opioids that are coming through the mail, that they hardly have any chance to be looking at other illicit products that are coming through.

WICKER: You're not really blaming the Postal Service, are you?

SHELLEY: No.

WICKER: What about UPS and FedEx, do the same thing?

SHELLEY: The problem is that we have such a new business model from illicit traders that they're segmenting their markets, that it's just putting an enormous pressure on our delivery services to monitor these fragmented shipments of illicit items. It's a real national concern. And they're stepping up to the plate. They're not avoiding this issue, but it's just a massive problem to try and find the needles in the haystack.

WICKER: And you mentioned harmonization of tax policies.

SHELLEY: Right.

WICKER: So tell us about – what ought to be done there?

SHELLEY: I think that when you have such low taxes, such as you have in North Carolina – I'm not faulting North Carolina, I'm just saying we have those – and very high taxes in Michigan, there's an incentive to move cigarettes in bulk.

WICKER: But if we didn't – if we didn't tax cigarettes at all, this wouldn't really – we wouldn't have this problem of illicit trafficking of cigarettes.

SHELLEY: Right, but we need revenue. And cigarettes are a very good way to achieve revenue. So I don't think we want to de-tax cigarettes, both for a public health reason – as Mr. Sweanor will tell you more – and also for a revenue reason. But one of the things that we need to do is find what I call a balance between what provides revenue, what deters consumption, and – but what does not encourage movement to an illicit market.

WICKER: OK. And this is a global problem, which is why we're having an OSCE Helsinki Commission hearing on this.

SHELLEY: Yes.

WICKER: So what can be done at the OSCE level, at the EU level, at the international consultation and treaty level to address this harmonization of tax policies?

SHELLEY: I think –

WICKER: And you're advocating that, are you not?

SHELLEY: I'm advocating that we begin to have, you know, research and analysis – such as Mr. Sweanor is suggesting – and then that is applied in ways that help construct more rational and harmonized policy. One of the things that I talked about, at the OSCE there's an annual symposium for the ambassadors on the latest trends and tendencies and threats. And I was asked to speak on transnational threats, as opposed to many other issues that they've

discussed before. This year they decided that illicit trade, along with cybercrime, was a priority for them. And this was quite new to the OSCE, to think about these issues as central problems for them. But there was a lot of receptivity. And I think that's important. We didn't get into all of the nitty gritty, but I think that's important.

WICKER: Why is this a new – why is this a recent problem and phenomenon? Or have I misunderstood you on that?

SHELLEY: It's not a recent problem, but it's certainly – it's growing. And the fact that there are many more people in Europe who are not working in the legitimate economy through – either through the recession or through migration are not integrated into the legitimate economy. It's been shown that this illicit trade had funded terrorism in Europe, which Europol was not looking at until about two, three years ago.

WICKER: Really?

SHELLEY: Two, three years ago, they were not looking at the crime-terror relationship. In fact, I had discussions with the head of Europol, who headed this working group at the World Economic Forum, when I released my last book that looked at these relationships. And he said: We don't perceive this is a great problem. But it is one of – illicit cigarettes is one of the unifying points between the criminals and the terrorists, because it is such an under-policed area of activity. And now Europol has totally switched and is focusing multiple times an hour in their databases of reviewing these linkages between crime and terrorism. And I understand, from my discussions in France earlier this month, that the new minister of interior is very much focused on doing more network analysis of looking at these relationships and that there is going to be a real shift in policy.

WICKER: Whose minister of interior?

SHELLEY: Macron's new minister of interior has begun to focus on these issues of crime and terrorism relationships because France, as we've seen, is the – is the champion of the moment of this illicit trade in cigarettes.

WICKER: If we stamp it out in France, probably move someplace else.

SHELLEY: It may move something else, but it's also related – as Mr. Sweanor has said – to larger economic issues.

WICKER: OK. Well – now, I'm going to let you take a breath.

SHELLEY: Thank you.

WICKER: And ask if either panelist would like to weigh in on anything you've talked about so far. And then we're going to get to Mr. Sweanor's point about alternatives.

FIRESTONE: Well, sir, I would just add to what Dr. Shelley is saying. I think one reason that this topic gets maybe less attention is, as the title of this hearing calls it, "A Hazy Crisis." And there is haziness to it.

WICKER: We like that. I thought that was pretty clever. (Laughter.)

FIRESTONE: Yeah, it's – well, I will compliment you, sir, as the chairman, on having come up with it. I don't –

WICKER: Oh, I have a good staff.

FIRESTONE: Yeah, the good staff, (genius ?) staff.

But to all the creators of that phrase, I think it really does capture one of the great challenges here, is it is a hazy crisis in that there are so many thousands and thousands and thousands of people involved at different levels in the supply chain, in making the termite brands and transshipping them, et cetera, et cetera.

Another challenge – where there are solutions is the transnational nature of the problem, where by definition – well, it turns out most of the time we're dealing with transnational shipments, smuggling from country A to country B, and there are often questions about who has jurisdiction, even within the two countries, and how do those two countries integrate their enforcement efforts, how do they share information, et cetera, et cetera. So I would say that there are a lot of those process aspects that can make the enforcement more effective.

And then, third, I would add to the points you made in your hypothetical. If you had a condo in Maryland and were receiving cigarettes there illicitly, what would the penalties be? I think a problem to address is raise consumer awareness because ultimately all of these products in the illicit trade, whether termite brands or counterfeit, are going to actual individuals, and there needs to be a much greater sense among those individuals that this is not something to do, and that when you do this maybe you do save \$20, \$30 on your carton but those \$20-30 in savings are funding this enormous criminal activity around the world. And that's another aspect of demand reduction, along with Professor Sweanor's very interesting and important ideas about demand reduction by shifting people to better policies.

WICKER: OK, well, let's shift to that, then. Mr. Sweanor, tell us what you mean. I made a note here: it's the smoke that kills, not the nicotine. That just gets you addicted. The tobacco itself doesn't kill you. But – although I guess it could give you throat cancer. But you suggest that there are viable tobacco alternatives to smoking and we ought to look at that. So would you enlarge on that for us, please?

SWEANOR: Sure. We've known scientifically for decades, as the late Professor Michael Russell used to say, that people smoke for the nicotine but they die from the tar. They die from the smoke. It would be like trying to get our caffeine by smoking tea leaves rather than brewing them; we would get the same diseases. It's the smoke that's causing the cancers, the heart disease, the lung disease, anything that gets smoke into our bodies. You know, cooking

over an open fire without ventilation, you'll get the same diseases. Firefighters get diseases from inhaling smoke. We have examples such as in Sweden, where the primary form of tobacco use is a form of oral tobacco called snus, with minimal health risks. It's very hard to distinguish between snus users and non-tobacco users in terms of health outcomes, whereas cigarettes will kill over half of their long-term users.

WICKER: How do you consumer snus?

SWEANOR: It's something that one just puts between their lip and their gum. It's very similar to moist –

WICKER: They feel very relaxing.

SWEANOR: Yeah. Things like Copenhagen or Skoal, products that are in the United States as well, which are also –

WICKER: So is snus a snuff?

SWEANOR: Yeah. It's a moist snuff product made by –

WICKER: That's going to give me mouth cancer, isn't it?

SWEANOR: Apparently it doesn't. I mean, the best evidence is that it's not causing cancer. You can never prove something doesn't cause cancer, we just can't find evidence that it does.

WICKER: OK. Do they –

SWEANOR: And that's very different than cigarettes.

WICKER: Do they tax snus?

SWEANOR: They do, but they had the big switchover in the 1970s, when they had differential taxation so that the – a package of snus cost half as much as a pack of cigarettes and apparently lasted about twice as long, so your effective price is much lower. So very similar to what some countries did in moving from leaded to unleaded fuel.

WICKER: So there's not – there's not as much of an incentive to cheat because the taxes are lower.

SWEANOR: Yeah, there's a viable alternative. We see the same thing with –

WICKER: A viable alternative. But theoretically, if we – if we aggressively taxed snus, then we'd end up with the same problem of being able to buy it untaxed online and fund terrorism.

SWEANOR: Well, there is – there is a difference here, in that if you’re buying cigarettes, from a health standpoint – and I’m sure Mr. Firestone will agree with me – there’s really no difference between the things that are manufactured by the major companies, the major brands, and those termite-type brands. There are reasons why if, for instance, I offered you an EpiPen that I’ve just brought back from the night market in Asia, that you would decide you didn’t want to buy it because it’s counterfeit. There’s a reason you want something different. When a product’s made to exacting standards and you know that it’s much lower risk, there’s a reason why you want the legitimate product rather than something faked. If your children are sick and I offer you a fake pharmaceutical product at a much lower price, you’re probably going to tell me to take a hike.

So when we come up with far safer products, there’s reasons to buy the legitimate products, and that’s working with consumers. And with some of these products, they’re actually cheaper than the illicit cigarettes, as we’ve seen with vaping products in my own country of Canada, of people who have moved from illicit cigarettes to vaping to save money. They didn’t even know initially that, you know, as the Royal College of Physicians in the U.K. has told us, these products are likely to be at least 95 percent less hazardous than cigarettes. It’s just they’re way cheaper. But if we gave people the information to say not only are these products likely to be at least 95 percent less hazardous than smoking, they’re going to cost you less money than then even the contraband cigarettes, we get a – we go from a problem now where contraband is a public health problem as well as a criminal problem as well as a revenue problem to something where we do something that gets rid of the criminality while solving our biggest cause of preventable death. So we have a huge opportunity to seize here.

WICKER: Would people acknowledge that Sweden is a success story in combatting illicit cigarette smuggling?

SWEANOR: Yeah, I haven’t been to Sweden for a few years, but I used to go there quite frequently. I didn’t see a problem there, in part because, you know, as I say, the – this is a business, and it’s a matter of where’s your market, how big is the market, how much can you sell for. Well, we just recently had data out of Eurobarometer that said the daily smoking rate in Sweden is now down to 5 percent. There just aren’t a whole lot of people smoking cigarettes. If you’re going to try to sell cigarettes, far better that you go to a place like France or elsewhere where it’s over 30 percent.

WICKER: Well, that is remarkable because I can tell you, you walk down the street of a major city in most European countries and it’s graphic, the number of people that are walking up and down the sidewalks smoking.

Dr. Shelley, who’s doing a good job in the international community on this issue? Who can we look to for success stories?

SHELLEY: I think Mr. Sweanor has given us a success story in Sweden in reducing consumption, which helps reduce illicit trade. The British and Her Majesty’s Customs Service have allocated a lot of attention to trying to analyze the problem. They still have serious

problems of illicit trade, but they do prioritize this. And maybe Mr. Firestone can give us some other examples that he –

WICKER: Mr. Firestone, do you all make snus?

FIRESTONE: It's a very, very small part of our business. We're focused on – (microphone feedback) –

WICKER: Go ahead.

FIRESTONE: Yes, sir.

WICKER: Good news; they've called a vote.

FIRESTONE: Oh.

WICKER: So this hearing is almost over.

FIRESTONE: All right. No, this is – (chuckles).

We are on a completely new strategy at PMI, which is what we're calling designing a smoke-free future, and that really focuses on some of the types of products that Professor Sweanor mentioned, including heat-not-burn tobacco. And we have applications pending before the FTA right now on that.

In terms of countries, I wholeheartedly agree with Professor Shelley that the United Kingdom has been, I think, very focused and very thoughtful on this topic. From our perspective, we've also seen that Greece has been receptive to trying to address the problem, as well as Poland. Even though Poland is a source of product that goes west into the higher-priced markets, we have had good experiences in cooperating with the Polish government as well.

WICKER: Well, let me just say this has been a real education to this senator, and I appreciate the testimony and the give-and-take with the witnesses.

One thing that always bothers me in a hearing is you've got this pesky chairman calling time on the questions. There was nobody to do that to me today, so we went on and on and we had a nice exchange.

There have been so many conflicts with our members. We had – we had four who were going to try to attend and ask questions. And regrettably Senator Boozman had to leave after hearing the testimony, but I know he appreciated the testimony.

But the word goes out, whether there are members here to ask questions or not. And I think we've made a valuable point today. If you're out there and you think you're going to save 20 (dollars) or 30 (dollars) or \$50 on this illegal, illicit product, you're engaged in something a lot bigger and you're funding some of the worst actors that have ever walked the face of the

Earth. And to that extent, bringing public attention and understanding to this has been very helpful.

We need to continue a dialogue on the role of government, the role of a legislative body and our oversight, our statutory pronouncements. And I look forward to hearing more from the three of you in the future – feel free to substitute additional testimony and supplement your answers – and also from the public.

And with that, and with the thanks of the Commission, this hearing is adjourned.
(Sounds gavel.)

[Whereupon, at 10:38 a.m., the hearing ended.]