

Understanding the U.S. Illicit Tobacco Market

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ISSUE BRIEF

Lessons from International Experiences

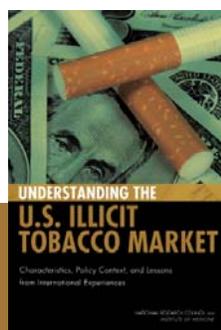
Although tobacco use has declined in recent decades, worldwide more than one billion people still regularly use tobacco, including many who purchase cigarettes outside legal markets. Illicit tobacco markets can deprive governments of tax revenue and undermine public health efforts to reduce tobacco use. To answer a number of questions about the illicit tobacco market, a committee of experts appointed by the National Research Council and Institute of Medicine conducted a study and released its findings in the report *Understanding the U.S. Illicit Tobacco Market*.



One question examined in the report is whether other nations' experiences in combatting illicit markets have yielded lessons that could be applied in the United States. International efforts to combat the illicit tobacco trade have focused on measures that target large-scale smuggling across international borders, a form of the trade that appears to be a relatively small problem in the United States. Nevertheless, the broad-ranging interventions adopted by other nations are instructive because they show that it is possible to reduce the size of the illicit tobacco market by dedicating resources for enforcement, collaborating across jurisdictions, and implementing strategies that use a variety of regulatory, enforcement, and policy approaches.

United Kingdom. In 2000, authorities estimated that one of every five cigarettes smoked in the UK was illicit, amounting to 3 billion pounds in lost tax revenue annually. In response, law enforcement authorities enhanced their anti-smuggling enforcement efforts, hiring additional staff to strengthen investigation and intelligence efforts and imposing tougher penalties for smugglers and sellers of illicit goods. The UK also required that cigarette packs be marked when duty was paid so that illicit products could be easily identified. They entered into memorandum of understanding agreements with three of the UK's major cigarette manufacturers, enlisting their support in controlling the supply of cigarettes to the illicit market. Specific measures were also taken to combat counterfeiting and the smuggling of illicit whites into the country, including requiring covert anti-counterfeiting markings on cigarette packs and devoting enforcement resources to intercept contraband overseas before it entered the UK market.

Between 2000 and 2013, the size of the UK's illicit market fell from 21 percent of the total tobacco market to 9 percent. UK customs credits the strategy's success to the development of local and regional partnerships and the ability of law enforcement to alter its practices in response to shifts in the illicit market, reflected in the periodic renewal and revision of the tobacco action plan.



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Characteristics, Policy Context, and Lessons
from International Experiences

NATIONAL RESEARCH COUNCIL AND
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Spain. In 1995, contraband cigarettes accounted for nearly 15 percent of the Spanish market, even though the country had some of the lowest cigarette prices in Europe. The illicit cigarettes entered the country and other European nations through Andorra, with the complicity of the tobacco industry. Spanish authorities allocated resources—nearly 40 million Euros—to combating the problem. They also developed international partnerships and engaged authorities from the European Anti-Fraud Office and other European nations in collaborative actions, including preventing container smuggling, sealing the Andorran border, and introducing tougher anti-smuggling laws in Andorra. As a result, by mid-1999 illicit tobacco accounted for only a 5 percent share of Spain’s total market, a two-thirds reduction.

Canada. In the late 1980s and early 1990s, Canada’s illicit tobacco market was supplied by legally manufactured Canadian cigarettes exported to the United States and illegally smuggled back into Canada. This large-scale smuggling—which diverted untaxed in-transit cigarettes to the illegal market—was estimated to account for 30 percent of the total tobacco market. To combat this type of smuggling, the Canadian government enacted an export tax on cigarettes and negotiated settlements with the tobacco industry, which was largely complicit in the illicit activity. As a result of these interventions, the characteristics of the illicit market shifted from one dominated by large-scale smuggling to its current form—mainly comprised of the tax-free sale of cigarettes manufactured on Native reserves to non-Native reserve members, and to a lesser extent counterfeit cigarettes from abroad.

In response, a number of provinces placed control measures on distributors and retailers on Native reserves to help ensure that tax-exempt cigarettes are not sold to non-Natives. In addition, the Royal Canadian Mounted Police implemented an enforcement strategy aimed at dismantling illegal manufacturing facilities, disrupting supply lines, apprehending key figures, and confiscating trucks and boats used in smuggling. While the impact of the strategy has not been systematically evaluated, by 2010, Canada had reduced the illicit share of its market from nearly 30 percent in the 1990s to between 7.6 percent and 14.7 percent.

The Effectiveness of Comprehensive Strategies

Governments have opportunities to reduce the size of the illicit tobacco market by targeting particular points of diversion and by undermining the conditions that make the illicit tobacco trade possible. International experiences demonstrate that many possible policy interventions and enforcement approaches can be implemented for this purpose—and that the challenges presented by the illicit tobacco trade are not unique or insurmountable.

Understanding other nations’ experiences can provide important insights into the nature of the U.S. illicit trade, challenges that may arise in the future, and the effectiveness of policy interventions that may be adopted in response. If regulation of cigarettes in the United States spurs demand for illicit products, the nation’s illicit tobacco market could change, leading to new market characteristics—for example, illegal imports may become a greater problem—and new points for intervention, such as border and customs enforcement. Findings from international experiences can contribute to understanding and responding to such changes in the United States.

A more in-depth discussion of international experiences can be found in the report *Understanding the U.S. Illicit Tobacco Market: Characteristics, Policy Context, and Lessons from International Experiences*, available from the National Academies Press (<http://www.nap.edu>). The study was sponsored by the U.S. Food and Drug Administration. Any findings, conclusions, or recommendations expressed in this publication are those of the study committee and do not necessarily reflect those of the sponsor.