

Tobacco smuggling

**BRIEFING PAPER
DIVERSION BRANCH
AUGUST 26, 1997**

Criminal tobacco trafficking usually occurs when foreign governments or state governments impose a higher excise tax on tobacco products than found in surrounding jurisdictions. These tax disparities lead to large-scale tobacco (cigarette) diversion from a lawful to an unlawful destination, thus defrauding the state or foreign governments of their due revenue.

There has been an over 500% increase from 1992 to present in the number of contraband cigarette trafficking tobacco investigations that ATF is conducting. The recent rise in trafficking is attributable to a number of factors, most notably a significant increase in both Canadian federal and provincial tobacco taxes in the late 1980s/early 1990s and an increase in certain states' cigarette taxes. Intelligence has determined that there exists a network of traditional and nontraditional organized crime groups operating transnationally. ATF is working approximately 65 investigations involving Canadian/U.S. and Mexican/U.S. cigarette trafficking, low-state-to-high-state trafficking, and Native American illegal sales.

Canada's initial tax increase was an attempt to generate health care revenue and to decrease cigarette consumption. The criminal diversion of tobacco products into Canada evolved from small, individual smuggling activities into sophisticated criminal enterprises. Canadian/U.S. criminal organizations have defrauded the Canadian government of between one and two billion dollars in revenue per year. ATF, IRS, US Customs and other Federal agencies recently indicted 21 individuals allegedly involved in Canadian/U.S. alcohol/tobacco

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trafficking to Canada. Assets from this illegal activity are estimated at over \$500 million. In a similar scenario, higher state taxes in the Southwest has brought about U.S./Mexican diversion involving U.S. cigarettes "for export only." Export cigarettes are exempt from Federal taxes.

In the low-state-to-high-state trafficking, Michigan shows the greatest loss of state revenue with a conservative estimate of \$75 million per year. Michigan has the third highest cigarette taxes in the U.S. Michigan traffickers obtain illegal cigarettes from wholesalers and retailers located throughout the South, where tobacco is traditionally taxed at a lower rate.

ATF is also working in conjunction with state revenue and law enforcement authorities investigating illegal Native American cigarette sales to non-Native Americans. Native American cigarette tax structure varies by state although the supplier of cigarettes involved in the trafficking have been from out-of-state wholesalers. Smoke shops making illegal tax-free sales in New York, Oklahoma, Arizona, New Mexico, Washington state and Montana have been identified.

ATF is conducting ongoing liaison with other foreign law and revenue enforcement authorities to ascertain the scope of cigarette trafficking worldwide. ATF is also currently working with criminal investigators and tax officials in East European countries to develop tobacco regulations and also establish criminal enforcement in this area. For more information contact Chief, Diversion Branch, (202)927-8210.

Salient Points

Statistics in article citing extent of contraband trafficking are too high.

Some companies within the Tobacco Industries appear knowledgeable about contraband trafficking. HOWEVER, corporate structure with International and Domestic Offices/Companies, appear in direct competition, i.e, a domestic office will be hurt by trafficking because it competes with their distribution system. ATF has worked with R.J.Reynolds, Philip Morris, etc. to obtain prop cigarettes, etc, and met to discuss counter-trafficking measures.

Created Diversion Branch to focus primarily on A/T criminal activity.

24-hr Cigarette Hotline to report thefts and hijacking of shipments involving 60,000+ cigarettes. (Established with ATF and the Federation of Tax Administrators)

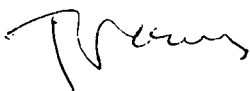
Alcohol and Tobacco Database to track diversion and trafficking activity based on ATF criminal and regulatory investigations

Creating Diversion Assistance Team (DAT) composed of Special Agents, Inspectors, Auditors, and Intelligence personnel to assess and assist in diversion investigations

In 1996, ATF seized \$804,373 in alcohol and tobacco, arrested 97 subjects, obtained 24

indictments, and obtained 6 successful prosecutions.

Criminal and civil violations include Internal Revenue Code (IRC), the Contraband Cigarette Trafficking Act (CCTA), Jenkins Act (not under our jurisdiction), and statutes relating to commerce with Indians, wire and mail fraud, money laundering, conspiracy and the Racketeer Influenced and Corrupt Organizations (RICO).



EFFORTS BY THE UNITED STATES CUSTOMS SERVICE TO COMBAT THE SMUGGLING OF CIGARETTES.

BACKGROUND

The United States Customs Service is the primary agency combating the smuggling of prohibited items into and out of the United States. One such item is contraband cigarettes. Presently, there are very few restrictions as to the amount of cigarettes that may be exported or sold domestically. As a result, many U.S.-made cigarettes are sold to U.S. exporters who sell the cigarettes to tobacco traders in foreign countries. Many of these sales are legitimate and the foreign countries involved are collecting the duties owed them. Due to high excise taxes and import quotas, however, many known cigarette traders sell their cigarettes on the black market for a fraction of the cost of retail cigarettes or smuggle them to other foreign countries. In so doing, cigarette smugglers are reaping huge profits.

This type of criminal activity has had some negative effects outside of U.S. borders. The taxes imposed on cigarettes in foreign countries are a great source of revenue. As more cigarettes are sold on the black market, tax revenues decrease. As the price of cigarettes decrease, moreover, more people are likely to smoke since the price is no longer a factor. This in turn will increase the financial burden on the health systems in those countries.

The Customs Service stepped up its efforts to combat smuggling on both a domestic and international level. On a domestic level, the presence of Customs at the ports of entry has increased in an overall effort to strengthen border interdiction. One residual effect of this fortification should be an enhanced ability to combat cigarette smuggling. In addition, the problem of cigarette smuggling has been brought to the attention of Customs personnel and the Department of Justice.

DOMESTIC EFFORTS

On June 23, 1997, 11 individuals were arrested as a result of a joint enforcement action executed by the Customs' Buffalo field office as part of a federal task force. Those participating in the arrests were the BATF, the IRS, the INS, New York State Police, the US Attorney's Office and the Royal Canadian Mounted Police (RCMP). This investigation, the subsequent initiation of the federal task force, and the formation of a special federal grand jury were predicated upon information developed by Customs' Resident Agent in Charge, Rouses Point, New York.

The resulting enforcement action stemmed from an indictment returned in the Northern District of New York charging 21 individuals with the following charges: money laundering; smuggling; conspiracy; wire and mail fraud; RICO; and unlawful introduction of liquor into Indian country. The indictment is a result of a two and one-half year joint investigation into the alleged money laundering activities of the Larry Miller organization and the Akwesasne Indian reservation. According to information received, Miller's organization allegedly diverted cigarettes and liquor to Canada through the Akwesasne Indian reservation and then

illegally transported unreported Canadian currency back into the US. During the course of the investigation, the Miller organization is alleged to have laundered over \$500 million. It is also believed that Miller invested heavily in Russian casinos and has ties to Russian organized crime. The indictment also seeks forfeiture of \$478,061,239 as well as substitute assets acquired by the defendants. In addition, seizure warrants were issued for ninety-nine vehicles, boats, snowmobiles, and other mobile conveyances. Also, Lis Pendens were filed against twenty-six real properties valued at approximately \$4 million. The investigation is continuing and additional arrests are expected.

In another case in which four defendants recently were sentenced, a shipment of 150 cases of Canadian manufactured cigarettes was seized in Louisiana by Customs in 1993. According to the information received, the cigarettes were destined for Canada in violation of U.S. Customs law. The investigation revealed that the cigarettes entered the U.S. from Canada and were being smuggled back into Canada in an attempt to circumvent Canadian excises taxes. This long-term cigarette smuggling investigation resulted in the sentencing, on July 30, 1997, of four defendants involved with the Brown and Williamson Tobacco Corporation. The investigation is continuing.

INTERNATIONAL EFFORTS

On an international level, there has been an increase in cooperation between the U.S. and foreign governments through more effective communication, as well as through the execution of additional Customs Mutual Assistance Agreements. The Office of Foreign Operations at Customs Headquarters has contacted the appropriate foreign attaches in an effort to further assist our foreign counterparts. Among the countries that have expressed an interest are France, Italy, Germany, and the Newly Independent States of the former Soviet Union.

Customs has and will continue to assist other countries on this matter. As a result of heightened cooperation between the Customs Service and foreign governments, a number of cooperative investigations have been initiated with our foreign attaches. Through continued dialogue and training of foreign law enforcement officers, foreign countries presumably will be better equipped to identify smuggling patterns and activity. More importantly, it is hoped that foreign law enforcement agencies identify the means by which these criminal enterprises launder their ill gotten gains.

Opening Statement
John W. Magaw
Director
Bureau of Alcohol, Tobacco and Firearms
before the
House Commerce Committee

*Tobacco
Smuggling*

December 9, 1997

Thank you, Mr. Chairman, members of the Committee. I appreciate this opportunity to better acquaint you with ATF's mission, and specifically, its role in preventing and investigating tobacco diversion.

History

For those of you not familiar with the Bureau's functions, let me tell you briefly a little about ATF's mission. In 1791, the nation's first tax was imposed on distilled spirits. This tax led to an uprising known as the Whiskey Rebellion, to which Treasury Secretary Alexander Hamilton dispatched the militia to put down the uprising. Over the years, ATF, and its predecessor, the Alcohol and Tax Unit of the Internal Revenue Service (IRS), has been charged by Congress with the regulation, taxation and criminal enforcement jurisdiction over violations of firearms, explosives, alcohol and tobacco laws.

The common thread in ATF's responsibilities over these varied products is they all are both legal commodities produced by a highly regulated industry and are also controversial products that have been traditionally susceptible to criminal diversion and misuse or abuse.

Mission

ATF's mission is three-fold: to reduce violent crime; to collect revenue; and to protect the public. We accomplish this with an integrated approach using regulatory inspectors, auditors, chemists, criminal investigators, and other specialists. And might I add, we are very good at what we do. For the past two years, ATF has been awarded the highest rating possible on its annual CFO audits by the Treasury Inspector General. We have learned from years of experience that, in many cases, voluntary compliance by the regulated industry can be achieved and criminal misuse and diversion can be prevented by regulatory oversight. The area of tobacco diversion is a prime example of the interactive nature of ATF's resources and authority. Ensuring that the industry is complying with regulatory and tax requirements can help prevent criminal diversion.

Jurisdiction

In 1978, Congress passed the Contraband Cigarette Trafficking Act, giving ATF the authority to investigate interstate diversion of cigarettes in avoidance of paying state tax, by prohibiting the shipment, transportation, or possession of more than 60,000 cigarettes (which equates to 3,000 packs or 300 cartons) not bearing indicia (or tax stamp) of evidence of tax payment in States that require such evidence. With this and other statutes, ATF's mandate to assist state and local governments has become a significant part of its mission. Originally enacted to prevent sales on the street, the problem of cigarette smuggling has become large commercial operations resulting

in these cigarettes ending up on retail shelves and distribution by organized crime.

Other statutes which can be applied in these cases include the Internal Revenue Code (IRC) and the Racketeer Influenced and Corrupt Organizations Act (RICO). ATF's goal is to achieve compliance with U.S. laws and to close the avenues to those involved in illegal diversion.

Extent of the Problem

In recent years, some foreign governments and certain state government have imposed a higher excise tax on tobacco products, thus creating a lucrative black market. Diversion involves products for both export and domestic consumption from a manufacturer to individuals acting as a broker or wholesaler. Rather than shipping the product to the destination stated on required Federal records, the product is diverted and sold illegally. Traceability is lost as goods disappear from legal commerce. Some wholesalers have been found to be the sources of supply, with retailers becoming increasingly active in these illegal sales. Unlike tobacco manufacturers, tobacco wholesalers and retailers are not statutorily required to hold permits and licenses issued by ATF.

For example, due to extremely high Canadian taxes on tobacco, significant quantities of U.S. manufactured tobacco products are smuggled into Canada. In addition, large amounts of Canadian manufactured tobacco products are "exported" into the United States and then smuggled back into Canada. As a result of this smuggling, Canada has lost billions of dollars in

tax revenues.

In addition, there has been a significant increase in trafficking in cigarettes from States with low taxes on tobacco to States with high taxes on tobacco. In a survey ATF conducted earlier this year on behalf of the House Appropriations Committee, ATF received estimates from several states on revenue loss figures. The State of Michigan estimated losing approximately \$50 million a year to cigarette diversion. The State of Washington estimated losing around \$100 million per year from cigarettes diverted from low tax states. California estimates its annual loss to be approximately \$30 million a year. The full extent of loss nationwide is difficult to calculate as many states polled were unable to give an estimate of their annual losses.

To give you an idea of ATF's involvement in diversion cases, we currently have over 85 open alcohol or tobacco trafficking investigations. Although limited resources put limitations on the number and extent of the investigations ATF undertakes, our investigations have increased over 500 percent in the past five years. Since 1994, ATF has made assessments of over \$30.4 million from companies and individuals involved in tobacco and alcohol trafficking. Seizures of tobacco commodities in 1997 totaled \$1.1 million.

ATF's largest contraband cigarette trafficking investigation involved the trafficking of cigarettes from the state of Montana -- the Flathead Indian Reservation -- to Washington state. In this case, six persons were convicted of racketeering, and three persons pleaded guilty to Conspiracy to Commit Racketeering. The average jail time was three years, and the maximum was 12 to 15

years. Total penalties were \$4.7 million and this sum was split between the U.S. government, the states, and the tribes.

ATF has a current investigation open involving 21 persons indicted in New York as part of a joint ATF, RCMP, U.S. Customs, INS, IRS and New York State Enforcement investigation. This investigation involved a smuggling ring on the St. Regis Mohawk Indian Reservation. Those indicted include prominent Native Americans from the St. Regis/Akwesasne Reservation and individuals associated with a Buffalo organized crime family. The charges include money laundering and racketeering. The assets from illegal proceeds are in this case estimated at over \$500 million.

In addition to illegal trafficking by traditional organized crime groups and Native Americans, ATF has also uncovered involvement in cigarette smuggling by Russian, Middle Eastern, and Asian organized crime groups. Investigation has revealed that these groups are also involved in firearms and narcotics trafficking, alien smuggling, and other illegal activities.

Over the past several years, alcohol and tobacco crimes have grown larger and more complex and have extended to both interstate and international investigations. Diversion cases often include nationwide activities since the smuggled goods are acquired in one part of the country and may be distributed unlawfully in another far away part of the country. In recognition of this national scope, ATF has established a Diversion Branch in Bureau Headquarters to coordinate and monitor these investigations. An Alcohol and Tobacco Database has also been developed to

track diversion and trafficking activity.

Due to a substantial loss of revenue and a heightened awareness, many states have requested ATF's assistance in helping to eliminate this problem. Through our efforts to eradicate this problem, ATF, in cooperation with the Federation of Tax Administrators, has established a 24-hour cigarette hotline, 1-800-659-6242, to report stolen, hijacked or seized cigarettes. You can be assured of our commitment to assisting state and local governments in their efforts to combat cigarette diversion.

On the international level, ATF maintains ongoing liaison with foreign law and revenue enforcement authorities, such as the Royal Canadian Mounted Police (RCMP) and Revenue Canada, to ascertain the scope of cigarette trafficking worldwide. The Bureau also is working closely with criminal investigators and tax officials in East European countries to develop and implement criminal and regulatory enforcement schemes with respect to cigarettes.

Finally, ATF has worked, through the issuance of Industry Circulars and meetings, to ensure that legitimate members of the tobacco industry do not facilitate illicit tobacco trafficking.

Thank you, again, for the opportunity to appear before your committee today. I would be happy to answer any questions you may have.

Draft language regarding tobacco product labeling and advertising abroad

SEC. 1. EXPORTS OF TOBACCO PRODUCTS ABROAD

(1) **REQUIREMENTS** --It shall be unlawful for any domestic concern to export from the United States, or to sell or distribute in, or export from, any other country, any tobacco products the package of which does not contain a warning label that--

(A) complies with Federal labeling requirements for cigarettes manufactured, imported, or packaged for sale or distribution within the United States; and

(B) is in the primary language of the country in which the cigarettes are intended for consumption.

(2) **WAIVERS** --The President may waive the prohibition contained in paragraph (1) if the President determines that the country in which the exported tobacco products are intended for consumption has in effect requirements for labeling of tobacco product packages substantially similar to or more stringent than the requirements for labeling of tobacco products set forth in paragraph (1).

SEC. 2. ADVERTISING OF TOBACCO PRODUCTS ABROAD

(1) **REQUIREMENTS** --It shall be unlawful for any domestic concern to advertise or cause to be advertised abroad any tobacco product in a manner that does not comply with Federal requirements for the advertisement of tobacco products in the United States.

SEC. 3. PENALTIES.

(1) **FINE** --Any person who violates the provisions of section 1 or section 2 shall be fined not more than \$100,000 per day for each such violation. Any person who knowingly reexports from or transships tobacco products through a foreign country for which the President has issued a waiver as described in section 1(2) to avoid the requirements of section 1 shall be fined not more than \$150,000 per day for each such occurrence.

(2) **INJUNCTION PROCEEDINGS** --The district courts of the United States shall have jurisdiction, for cause shown, to prevent and restrain violations of section 1 or section 2 upon the application of the Attorney General of the United States.

SEC. 4. DEFINITIONS.

(1) **DOMESTIC CONCERN** --In this act, the term "domestic concern" means--

(A) any individual who is a citizen, national, or resident of the United States; and

(B) any corporation, partnership, association, joint-stock company, business trust, unincorporated organization, or sole proprietorship which has its principal place of business in the United States, or which is organized under the laws of a State of the United States or a territory, possession, or commonwealth of the United States.

*substantive
conclusion*

ECPA

Memorandum

To: Int'l tobacco working group
From: Cathy Carpino
Date: December 18, 1997
Subject: Outline of anti-smuggling proposal

I. Establish a permit system for cigarettes: Mirroring the system in place for alcohol (27 USC 203, et seq), this proposal would require any person engaged in the business of manufacturing, distributing, selling, or importing tobacco to obtain a permit from the Treasury Secretary within a certain period of time (e.g., 180 days) of enactment of Act. Any person shall be entitled to a permit unless they have been convicted of a felony, convicted of a misdemeanor involving tobacco within the past three years, or if such person is unlikely to conform their operations with federal law.

The Secretary may suspend, revoke, or annul a permit if any of the permit's conditions are violated. These permits cannot be transferred voluntarily. If transferred by operation of law, the new permittee shall have 30 days within which to reapply. The old permit shall continue in effect until the Secretary acts on the permittee's application.

To prevent the sale or distribution of cigarette packages that do not comply with federal labeling requirements, no person shall produce, distribute, or sell cigarettes unless that person obtains a certificate from the Secretary. Officers of internal revenue are authorized and directed to withhold the release of packages of cigarettes from the manufacturer unless such a certificate has been obtained. Customs officers are authorized and directed to withhold the release of packages of cigarettes from customs custody unless certificates have been obtained. [need to look at the Kennedy bill and Conrad's proposal to ensure consistency]

II. New labeling requirements for cigarette packages: (1) The President is directed to require cigarette manufacturers to identify the manufacturing facility, distribution facility, export warehouse, and any other information determined by the President to be relevant to the chain of custody on each package of cigarettes within one year of enactment of this Act. The stamp containing this information shall use secure technology that is not susceptible to

alteration, but that can be accessed by officials, both in the United States and in foreign countries, and (2) Cigarette manufacturers shall label every package with the country of final destination. The President shall promulgate regulations regarding the size and location of this stamp on the package. If manufacturers do not comply with federal labeling requirements, the Secretary of Treasury shall revoke their permit, in addition to applying all existing penalties.

III. Tracking requirements: (1) Cigarette manufacturers are required to post a bond for exported packages of cigarettes to be returned when the Secretary of Treasury receives documentation that such cigarettes reached their final destination. The Secretary of Treasury shall promulgate regulations determining the amount of the bond and what documentation is needed to verify delivery of the packages; (2) in order to obtain the return of a bond, the Secretary shall determine that a country has a legitimate market for cigarettes exported from the United States and that such cigarettes are to be consumed in that country as part of the legitimate market. The Secretary shall publish the list of these countries; and (3) Cigarette manufacturers cannot sell to any person, either in the United States or in a foreign country, if they have reason to believe such person will violate any law or regulation of that country, or if such person was convicted of a crime involving cigarettes.

IV. Military bases: The Secretary of Defense is directed to require that packages of cigarettes sold overseas on military bases shall be priced at the highest level found in the country in which the base is located or in the United States, whichever is greater. Packages of cigarettes sold on military bases shall be so marked.

V. Indian reservations: Packages of cigarettes on Indian reservations shall be so marked.

VI. Duty-free stores: Duty-free stores located in the United States shall not sell packages of cigarettes and no person in the United States may sell to duty-free stores in foreign countries.

VII. Increased resources: It is the sense of the Senate that the Treasury Department shall allocate additional resources to curb the problem of cigarette smuggling, especially on Indian reservations.

AMERICAN CENTER FOR A TOBACCO-FREE WORLD

Sec. I FINDINGS

1) Tobacco use is estimated to have caused nearly 3 million deaths a year worldwide in the early 1990's, and is projected to cause in excess of 10 million additional deaths a year globally by 2025, making it the leading killer worldwide. More than 70% of those deaths are expected in developing countries

2) Most developing governments are unprepared to address increases in tobacco deaths, including the impact on health systems and health costs. Very few have implemented the fiscal and regulatory policies that can limit increases in tobacco attributable deaths. While tobacco consumption in the U.S. and other established market economies has fallen over the last decade, consumption is rising in China, India, East Asia, and former socialist economies. Tobacco companies in the US and elsewhere have increasingly targeted these markets. ~~Along with China, Germany, and Japan, the US accounts for one-half of the global cigarette production.~~

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How much 11.5?

3) Tobacco use markedly reduces good health and threatens to erode the major health gains in life expectancy of the last century. Only HIV infection and tobacco are large and growing causes of death worldwide. The total projected deaths from tobacco over the next ten years likely will exceed deaths from HIV, maternal and childhood conditions and tuberculosis combined. ~~While the US has shown significant leadership in mobilizing international HIV control, it has done far less to prevent the spread of tobacco use.~~

4) ~~Since 1992, the World Bank has adopted a formal policy of not lending for tobacco production, processing, or marketing. The World Bank's conservative estimate is that tobacco investment globally resulted in an annual \$200 billion net economic loss around 1990. Any economic evaluation that places reasonable value on human life suggests a net loss from tobacco.~~

5) ~~The adoption of comprehensive national legislation governing tobacco will constitute necessary world leadership. No civilized society can do less to stem the toll of disease and death from tobacco use. Since marketing abuses that the US seeks to control at home are practiced without restraint abroad by US-based companies, there is both a public health and moral obligation to do the extent possible to see that the protections afforded US citizens are extended to all.~~

5) The United States consistently has provided leadership and funding to address the world's most pressing public health needs, including AIDS, hunger, maternal and child health, and immunization. (Annual U.S. funding for these public health issues exceeds \$XXX)

6) The United States exports more than 240 billion cigarettes per year worth more than \$6 billion. The leading American tobacco company made in excess of \$6.3 billion in overseas profits in 1996, ranking third in performance among transnational US-based companies. Foreign sales now account for more than half of all sales for the two leading

U.S. tobacco manufacturers.

7) In light of the role the U.S. has played in spreading tobacco use globally, and in light of the large financial benefits the U.S. continues to enjoy from tobacco exports, it is appropriate that this nation provide significant assistance and funding for international public education and mass media programs that inform the public about the hazards of tobacco use.

8) Smoking in U.S. films is pervasive and influences persons in other countries who seek to emulate "American activities" depicted in motion pictures. A recent study recently reported that more than half of the top-grossing U.S. films released between 1991 and 1996 exhibited smoking. In these films, 80 percent of the male lead characters and 27 percent of the female characters smoked. The motion picture industry is painting a distorted picture that smoking is a truly American activity.

~~6) Remuneration for the death and disease caused by these profits is appropriate. At the very least, American policies governing advertising, production, labeling, packaging and sales at home must be consistent abroad.~~

SEC. 2 PURPOSES. The American Center for a Tobacco-free World (ACT) shall assist organizations in other countries to address the several health problems associated with tobacco use through-

1) public education programs that inform the public about the hazards of tobacco use and of environmental tobacco smoke,

2) mass media campaigns, including paid counter-tobacco advertisements, to reverse the image appeal of pro-tobacco messages, especially those that glamorize and "Westernize" tobacco use to young people,

3) educating organizations about the economic and societal costs of tobacco use, and effective tobacco use prevention strategies that are appropriate for the country;

4) facilitating access to nicotine addiction therapies,

5) evaluating ^{and disseminating} tobacco use cessation ^{or prevention} strategies, and

6) providing technical assistance to develop standardized epidemiologic methodologies to monitor tobacco use

7) and other efforts to reduce tobacco use

SEC. 3 DEFINITIONS.

(a) Trust fund _The term "Trust Fund" means the National Tobacco Settlement Trust Fund established in the Treasury of the United States consisting of amounts that are appropriated or accredited to the trust fund from the tobacco settlement approved by Congress

SEC 4. AMERICAN CENTER FOR A TOBACCO-FREE WORLD

Congress finds that there is established in the District of Columbia a private, nonprofit corporation known as American Center for a Tobacco-free World (ACT) which is neither an agency nor establishment of the United States Government

*901 c (3)
\$ of 400,000
with last
meeting*

SEC 5 FUNDING

(a) ESTABLISHMENT OF GLOBAL PUBLIC HEALTH AND EDUCATION RESOURCE ACCOUNT . There is established with the Trust fund the Global Public Health and Education Resource Account that shall be accredited with \$___ for each fiscal year.

(b) IN GENERAL _The Secretary of the Treasury shall, on October 1 of each fiscal year subsequent to the effective date of this Act, transfer \$___ million from the Global Public Health and Education Resource Account of the Trust Fund to the account of the ACT to carry out the activities authorized under this Act

(c) TERMINATION OF TRANSFER AUTHORITY _The authority of the Secretary to transfer funds from the Trust Fund shall expire on ____

SEC. 6 ELIGIBILITY FOR ANNUAL TRANSFERS FROM THE TRUST FUND

(a) Nothing in this Act shall be construed to make the ACT an agency or establishment of the United States Government, or to make the members of the Board of the ACT, or its employees, officers or employees of the United States

(b) OVERSIGHT The ACT and its grantees shall be subject to the oversight and supervision of Congress, and shall annually submit a report of it's activities to ____

(c) CONDITIONS ON ELIGIBILITY FOR FUNDING (basically track language in sec 504 of PL 98-164- National Endowment for Democracy)

SECTION 4. AMERICAN CENTER ON GLOBAL HEALTH AND TOBACCO

Congress finds that there is established in the District of Columbia a private, non-profit corporation known as the American Center (ACT) On Global Health and Tobacco which is neither an agency nor establishment of the United States Government.

ACT is governed by a Board of up to 25 members including:

1. On a bipartisan basis members of the Senate of the United States and of the House of Representatives.
2. The Presidents of American public health organizations.
3. The Presidents of American media, marketing and other non-government institutions and corporations.
4. Individuals active in education, public health, and other relevant activities.

ACT is to have an International Advisory Council. This Council consists of representatives from key global, regional and national public health organizations and leading individual educators and health professionals.

It is directed that ACT is to have a limited staff and to the maximum extent utilize the available experience and talents of existing American organizations to carry out its mandate. These include American non-governmental organizations with specialized international experience in health, education, media and tobacco.

SECTION 5. FUNDING

- (a) **ESTABLISHMENT OF GLOBAL PUBLIC HEALTH AND EDUCATION RESOURCE ACCOUNT.** There is established with the Trust Fund the Global Public Health and Education Resource Account that shall be accredited with \$150 million for each fiscal year.
- (b) **IN GENERAL.** The Secretary of the Treasury shall on October 1 of each fiscal year subsequent to the effective date of this Act, transfer \$150 million from the Global Public Health and Education Resource Account of the Trust Fund to the account of ACT to carry out the activities authorized under this Act.
- (c) **TERMINATION OF TRANSFER AUTHORITY.** The authority of the Secretary to transfer funds from the Trust Fund shall expire with the expiration of the Trust Fund.

SECTION 6. ELIGIBILITY FOR ANNUAL TRANSFERS FROM THE TRUST FUND.

- (a) Nothing in this Act shall be construed to make ACT an agency or establishment of the United States Government, or to make the members of the Board of ACT, or its employees, officers or employees of the United States.
- (b) **OVERSIGHT.** ACT and its grantees shall be subject to the oversight and supervision of Congress, and shall annually submit a report of its activities to the Congress.

(c) CONDITIONS FOR ELIGIBILITY FOR FUNDING.

a. Annual Payments from the Trust Fund may be made to ACT under this title only if ACT agrees to comply with the requirements specified in this section and elsewhere in this title.

b.1. ACT may only provide funding for programs of private sector groups and may not carry out programs directly.

2. ACT may provide funding only for programs which are consistent with the purposes set forth in Section 2.

Salary or compensation c.1. Officers of ACT may not receive any salary or other compensation from any source, other than ACT, for services rendered during the period of their employment by ACT.

Travel expenses. 2. If an individual who is an officer or employee of the United States Government serves as a member of the Board of Directors or as an officer or employee of ACT, that individual may not receive any compensation or travel expenses in connection with services performed for ACT.

Stock or dividends. d.1. ACT shall not issue any shares of stock or declare or pay any dividends.

2. No part of the assets of ACT shall inure to the benefit of any member of the Board, any officer or employee of ACT, or any other individual, except as salary or reasonable compensation for services.

Audits. e.1. The accounts of ACT shall be audited annually in accordance with generally accepted auditing standards by independent certified public accountants or independent licensed public accountants certified or licensed by a regulatory authority of a State or other political subdivision of the United States. The audits shall be conducted at the place or places where the accounts of ACT are normally kept. All books, accounts, financial records, reports, files, and all other papers, things, or property belonging to or in use by ACT and necessary to facilitate the audits shall be made available to the person or persons conducting the audits; and full facilities for verifying transactions with any assets held by depositories, fiscal agents, and custodians shall be afforded to such person or persons.

Report. 2. The report of each such independent audit shall be included in the annual report required by subsection (h). The audit report shall set forth the scope of the audit and include such statements as are necessary to present fairly ACT's assets and liabilities, surplus or deficit, with an analysis of the changes therein during the year, supplemented in reasonable detail by a statement of ACT's income and expenses during the year, and a statement of the application of funds, together with the independent auditor's opinion of those statements.

GAO audit. f.1. The financial transactions of ACT for each fiscal year may be audited by the General Accounting Office in accordance with such principles and procedures and under such rules and regulations as may be

prescribed by the Comptroller General of the United States. Any such audit shall be conducted at the place or places where accounts of ACT are normally kept. The representatives of the General Accounting Office shall have access to all books, accounts, records, reports, files, and all other papers, things, or property belonging to or in use by ACT pertaining to its financial transactions and necessary to facilitate the audit; and they shall be afforded full facilities for verifying transactions with any assets held by depositories, fiscal agents, and custodians. All such books, accounts, records, reports, files, papers, and property of ACT shall remain in the possession and custody of ACT.

Report to
Congress

2. A report of each such audit shall be made by the Comptroller General to the Congress. The report to the Congress shall contain such comments and information as the Comptroller General may deem necessary to inform the Congress of the financial operations and condition of ACT, together with such recommendations with respect thereto as he may deem advisable. The report shall also show specifically any program, expenditure, or other financial transaction or undertaking observed in the course of the audit which, in the opinion of the Comptroller General, has been carried on or made contrary to the requirements of this title. A copy of each report shall be furnished to the President and to ACT at the time submitted to the Congress.

Report to
President

Recordkeeping

g.1. ACT shall ensure that each recipient of assistance provided through ACT under this title keeps such records as may be reasonably necessary to fully disclose the amount and the disposition by such recipient of the proceeds of such assistance, the total cost of the project or undertaking in connection with which such assistance is given or used, and the amount and nature of that portion of the cost of the project or undertaking supplied by other sources, and such other records as will facilitate an effective audit.

Information
accessibility

2. ACT shall ensure that it, or any of its duly authorized representatives, shall have access for the purpose of audit and examination to any books, documents, papers, and records of the recipient that are pertinent to assistance provided through ACT under this title. The Comptroller General of the United States or any of his duly authorized representatives shall also have access thereto for such purpose.

Report to
President and
Congress.

h. Not later than December 31 of each year, ACT shall submit an annual report for the preceding fiscal year to the President for transmittal to the Congress. The report shall include a comprehensive and detailed report of ACT's operations, activities, financial condition, and accomplishments under this title and may include such recommendations as ACT deems appropriate. The Board members and officers of ACT shall be available to testify before appropriate committees of the Congress with respect to such report, the report of any audit made by the Comptroller General pursuant to subsection (f), or any other matter which any such committee may determine.

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ant to this section shall be set forth in a grant agreement between the Secretary of State and The Asia Foundation.

(b) If funds made available to The Asia Foundation pursuant to this title or pursuant to any other provision of law are, with the permission of the head of the Federal agency making the funds available, invested by the Foundation or any of its subgrantees pending disbursement, the resulting interest is not required to be deposited in the United States Treasury if that interest is used for the purposes for which the funds were made available. Interest

FUNDING

Sec. 404. There are authorized to be appropriated to the Secretary of State \$5,000,000 for the fiscal year 1983, \$10,000,000 for the fiscal year 1984, and \$10,000,000 for the fiscal year 1985 for grants to The Asia Foundation pursuant to this title. 22 USC 403.

TITLE V—NATIONAL ENDOWMENT FOR DEMOCRACY

National
Endowment for
Democracy Act

SHORT TITLE

Sec. 501. This title may be cited as the "National Endowment for Democracy Act". 22 USC 411
note.

NATIONAL ENDOWMENT FOR DEMOCRACY

Sec. 502. (a) The Congress finds that there has been established in the District of Columbia a private, nonprofit corporation known as the National Endowment for Democracy (hereafter in this title referred to as the "Endowment") which is not an agency or establishment of the United States Government. 22 USC 411

(b) The purposes of the Endowment, as set forth in its articles of incorporation, are—

(1) to encourage free and democratic institutions throughout the world through private sector initiatives, including activities which promote the individual rights and freedoms (including internationally recognized human rights) which are essential to the functioning of democratic institutions;

(2) to facilitate exchanges between United States private sector groups (especially the two major American political parties, labor, and business) and democratic groups abroad;

(3) to promote United States nongovernmental participation (especially through the two major American political parties, labor, business, and other private sector groups) in democratic training programs and democratic institution-building abroad;

(4) to strengthen democratic electoral processes abroad through timely measures in cooperation with indigenous democratic forces;

(5) to support the participation of the two major American political parties, labor, business, and other United States private sector groups in fostering cooperation with those abroad dedicated to the cultural values, institutions, and organizations of democratic pluralism; and

(6) to encourage the establishment and growth of democratic development in a manner consistent both with the broad concerns of United States national interests and with the specific

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requirements of the democratic groups in other countries which are aided by programs funded by the Endowment.

GRANTS TO THE ENDOWMENT

22 USC 4412.

Sec. 503. (a) The Director of the United States Information Agency shall make an annual grant to the Endowment to enable the Endowment to carry out its purposes as specified in section 502(b). Such grants shall be made with funds specifically appropriated for grants to the Endowment or with funds appropriated to the Agency for the "Salaries and Expenses" account. Such grants shall be made pursuant to a grant agreement between the Director and the Endowment which requires that grant funds will only be used for activities which the Board of Directors of the Endowment determines are consistent with the purposes described in section 502(b), that the Endowment will allocate funds in accordance with subsection (a) of this section, and that the Endowment will otherwise comply with the requirements of this title. The grant agreement may not require the Endowment to comply with requirements other than those specified in this title.

(b) Funds so granted may be used by the Endowment to carry out the purposes described in section 502(b), and otherwise applicable limitations on the purposes for which funds appropriated to the United States Information Agency may be used shall not apply to funds granted to the Endowment.

Restriction.

(c) Nothing in this title shall be construed to make the Endowment an agency or establishment of the United States Government or to make the members of the Board of Directors of the Endowment, or the officers or employees of the Endowment, officers or employees of the United States.

(d) The Endowment and its grantees shall be subject to the appropriate oversight procedures of the Congress.

(e) Of the amounts made available to the Endowment for each of the fiscal years 1984 and 1985 to carry out programs in furtherance of the purposes of this Act—

(1) not less than \$13,800,000 shall be for the Free Trade Union Institute; and

(2) not less than \$2,800,000 shall be to support private enterprise development programs of the National Chamber Foundation.

ELIGIBILITY OF THE ENDOWMENT FOR GRANTS

22 USC 4413

Sec. 504. (a) Grants may be made to the Endowment under this title only if the Endowment agrees to comply with the requirements specified in this section and elsewhere in this title.

(b)(1) The Endowment may only provide funding for programs of private sector groups and may not carry out programs directly.

(2) The Endowment may provide funding only for programs which are consistent with the purposes set forth in section 502(b).

Salary or compensation.

(c)(1) Officers of the Endowment may not receive any salary or other compensation from any source, other than the Endowment, for services rendered during the period of their employment by the Endowment.

Travel expenses.

(2) If an individual who is an officer or employee of the United States Government serves as a member of the Board of Directors or as an officer or employee of the Endowment, that individual may

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not receive any compensation or travel expenses in connection with services performed for the Endowment.

(d)(1) The Endowment shall not issue any shares of stock or

Stock or
dividends.

(2) No part of the assets of the Endowment shall inure to the benefit of any member of the Board, any officer or employee of the Endowment, or any other individual, except as salary or reasonable compensation for services.

(e)(1) The accounts of the Endowment shall be audited annually in accordance with generally accepted auditing standards by independent certified public accountants or independent licensed public accountants certified or licensed by a regulatory authority of a State or other political subdivision of the United States. The audits shall be conducted at the place or places where the accounts of the Endowment are normally kept. All books, accounts, financial records, reports, files, and all other papers, things, or property belonging to or in use by the Endowment and necessary to facilitate the audits shall be made available to the person or persons conducting the audit, and full facilities for verifying transactions with any assets held by depositories, fiscal agents, and custodians shall be afforded to such person or persons.

Audits.

(2) The report of each such independent audit shall be included in the annual report required by subsection (h). The audit report shall set forth the scope of the audit and include such statements as are necessary to present fairly the Endowment's assets and liabilities, surplus or deficit, with an analysis of the changes therein during the year, supplemented in reasonable detail by a statement of the Endowment's income and expenses during the year, and a statement of the application of funds, together with the independent auditor's opinion of those statements.

Report.

(f)(1) The financial transactions of the Endowment for each fiscal year may be audited by the General Accounting Office in accordance with such principles and procedures and under such rules and regulations as may be prescribed by the Comptroller General of the United States. Any such audit shall be conducted at the place or places where accounts of the Endowment are normally kept. The representatives of the General Accounting Office shall have access to all books, accounts, records, reports, files, and all other papers, things, or property belonging to or in use by the Endowment pertaining to its financial transactions and necessary to facilitate the audit; and they shall be afforded full facilities for verifying transactions with any assets held by depositories, fiscal agents, and custodians. All such books, accounts, records, reports, files, papers, and property of the Endowment shall remain in the possession and custody of the Endowment.

GAO audit.

(2) A report of each such audit shall be made by the Comptroller General to the Congress. The report to the Congress shall contain such comments and information as the Comptroller General may deem necessary to inform the Congress of the financial operations and condition of the Endowment, together with such recommendations with respect thereto as he may deem advisable. The report shall also show specifically any program, expenditure, or other financial transaction or undertaking observed in the course of the audit, which, in the opinion of the Comptroller General, has been carried on or made contrary to the requirements of this title. A copy of each report shall be furnished to the President and to the Endowment at the time submitted to the Congress.

Report to
Congress.

Report to
President.

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Recordkeeping.

(g)(1) The Endowment shall ensure that each recipient of assistance provided through the Endowment under this title keeps such records as may be reasonably necessary to fully disclose the amount and the disposition by such recipient of the proceeds of such assistance, the total cost of the project or undertaking in connection with which such assistance is given or used, and the amount and nature of that portion of the cost of the project or undertaking supplied by other sources, and such other records as will facilitate an effective audit.

Information accessibility.

(2) The Endowment shall ensure that it, or any of its duly authorized representatives, shall have access for the purpose of audit and examination to any books, documents, papers, and records of the recipient that are pertinent to assistance provided through the Endowment under this title. The Comptroller General of the United States or any of his duly authorized representatives shall also have access thereto for such purpose.

Report to President and Congress.

(h) Not later than December 31 of each year, the Endowment shall submit an annual report for the preceding fiscal year to the President for transmittal to the Congress. The report shall include a comprehensive and detailed report of the Endowment's operations, activities, financial condition, and accomplishments under this title and may include such recommendations as the Endowment deems appropriate. The Board members and officers of the Endowment shall be available to testify before appropriate committees of the Congress with respect to such report, the report of any audit made by the Comptroller General pursuant to subsection (f), or any other matter which any such committee may determine.

Foreign Missions Amendments Act of 1983.**TITLE VI--FOREIGN MISSIONS****SHORT TITLE**

22 USC 4201 note.

SEC. 601. This title may be cited as the "Foreign Missions Amendments Act of 1983".

REQUIREMENT FOR LIABILITY INSURANCE

SEC. 602. Section 6 of the Diplomatic Relations Act (22 U.S.C. 254e) is amended--

(1) in subsection (a) by striking out "President" and inserting in lieu thereof "Director of the Office of Foreign Missions in the Department of State";

(2) in subsection (b) by striking out "The President shall, by regulation, establish liability insurance requirements" and inserting in lieu thereof "The Director of the Office of Foreign Missions shall, by regulation, establish liability insurance requirements which can reasonably be expected to afford adequate compensation to victims and which are"; and

(3) in subsection (c) by striking out "President" and inserting in lieu thereof "Director of the Office of Foreign Missions".

ENFORCEMENT OF COMPLIANCE WITH LIABILITY INSURANCE REQUIREMENTS

SEC. 603. Title II of the State Department Basic Authorities Act of 1966 is amended by inserting after section 204 (22 U.S.C. 4304) the following new section:

ALCOHOL AND TOBACCO
DIVERSION AND CONTRABAND
TRAFFICKING



ALCOHOL & TOBACCO PROGRAMS
DIVERSION BRANCH

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OVERVIEW OF TOBACCO CONTRABAND TRAFFICKING

Criminal tobacco trafficking usually occurs when foreign governments or state governments impose a higher excise tax on tobacco products than found in surrounding jurisdictions. These tax disparities lead to large-scale tobacco (cigarette) diversion from a lawful to an unlawful destination, thus defrauding the state or foreign governments of their due revenue.

There has been an over 500% increase from 1992 to present in the number of contraband cigarette trafficking tobacco investigations that ATF is conducting. The recent rise in trafficking is attributable to a number of factors, most notably a significant increase in both Canadian federal and provincial tobacco taxes in the late 1980s/early 1990s and an increase in certain states' cigarette taxes. Intelligence has determined that there exists a network of traditional and nontraditional organized crime groups operating transnationally. ATF is working approximately 65 investigations involving Canadian/U.S. and Mexican/U.S. cigarette trafficking, low-state-to-high-state trafficking, and Native American illegal sales.

Canada's initial tax increase was an attempt to generate health care revenue and to decrease cigarette consumption. The criminal diversion of tobacco products into Canada evolved from small, individual smuggling activities into sophisticated criminal enterprises. Canadian/U.S. criminal organizations have defrauded the Canadian government of between one and two billion dollars in revenue per year. ATF, IRS, US Customs and other Federal agencies recently indicted 21 individuals allegedly involved in Canadian/U.S. alcohol/tobacco

trafficking to Canada. Assets from this illegal activity are estimated at over \$500 million. In a similar scenario, higher state taxes in the Southwest has brought about U.S./Mexican diversion involving U.S. cigarettes "for export only." Export cigarettes are exempt from Federal taxes.

In the low-state-to-high-state trafficking, Michigan shows the greatest loss of state revenue with a conservative estimate of \$75 million per year. Michigan has the third highest cigarette taxes in the U.S. Michigan traffickers obtain illegal cigarettes from wholesalers and retailers located throughout the South, where tobacco is traditionally taxed at a lower rate.

ATF is also working in conjunction with state revenue and law enforcement authorities investigating illegal Native American cigarette sales to non-Native Americans. Native American cigarette tax structure varies by state although the supplier of cigarettes involved in the trafficking have been from out-of-state wholesalers. Smoke shops making illegal tax-free sales in New York, Oklahoma, Arizona, New Mexico, Washington state and Montana have been identified.

ATF is conducting ongoing liaison with other foreign law and revenue enforcement authorities to ascertain the scope of cigarette trafficking worldwide. ATF is also currently working with criminal investigators and tax officials in East European countries to develop tobacco regulations and also establish criminal enforcement in this area. For more information contact Chief, Diversion Branch, (202)927-8210.

Distribution System of Distilled Spirits

The distribution system for distilled spirits is a three-tier system - the distilled spirits plant (DSP) is at the top, a wholesale liquor dealer (WLD), is in the middle, and the bottom tier is the retail liquor dealer (RLD), the retail store from where consumers make their purchases. Except for in the case of exportation, tax is generally due upon removal of the distilled spirits from the DSP.

A WLD is defined as every person who sells, or offers for sale, distilled spirits wines, or beer to another dealer. The WLD must meet the requirements of Federal law by obtaining a basic permit and paying Special Tax. WLDs are required to maintain daily records of receipt and disposition of distilled spirits in accordance with 27 CFR Part 194.

The bottom tier of the three tier system, the RLD, is defined as every person who sells, or offers for sale, distilled spirits, wine, or beer to any person other than a dealer. RLDs are not required to obtain a permit from ATF, however they must pay Special Tax. All RLDs are required by 27 CFR Part 194 to keep records of receipt for all distilled spirits, and records for the disposition of 20 wine gallons or more of distilled spirits. (Distribution of 20 wine gallons or more to an individual constitutes a sale to a dealer. Such individuals are required to have a wholesalers basic permit).

Exportation

Distilled spirits may leave the plant without payment of tax for exportation, provided certain export steps are followed. After submitting the required notice to the appropriate District Director, the spirits may be withdrawn for direct exportation to the foreign customer, or for transfer to a Customs Bonded Warehouse (CBW) or Foreign Trade Zone (FTZ) for subsequent exportation. Upon proof of exportation, the DSP is relieved from the applicable tax liability.

Distribution System of Cigarettes

After the manufacture of cigarettes, the general industry pattern is to ship packaged Federally tax paid tobacco products to public warehouses that serve all manufacturers. There are approximately 81 public warehouses across the country. Public warehouses are not regulated by ATF.

The cigarettes remain the property of the manufacturers while in the public warehouse and are removed only upon the manufacturer's instructions. The cigarettes are distributed to wholesalers (stamping agents), government installations, and other public warehouses in the warehouse's distributing area for subsequent distribution to consumers.

A wholesaler stamping agent (WSA) is defined as a business having the authority from a state to affix to cigarette packs evidence of the appropriate state tax. By affixing tax stamps to cigarettes, the business becomes a licensed agent of that state. The WSA usually sells the cigarettes to other wholesalers (non-stamping agents), subjobbers and retailers.

State tax exempt sales consist primarily of sales to military installations, Veterans Hospitals, and Indian reservations.

Exportation

Tobacco products may be exported tax-free directly from the manufacturer or from export warehouses (EW). Packages of cigarettes destined for exportation are required to be marked with the statement "Tax-exempt. For use outside the U.S." or, "U.S. Tax exempt. For use outside the U.S." The tax liability is relieved once the manufacturer or export warehouse proprietor provides ATF with proof of exportation.

EWs are regulated by ATF, and they are required to obtain a permit, a bond and pay special tax. EWs generally receive tobacco products straight from the manufacturer, however, some are received from other export warehouses. Cigarettes travel in bond to the EW. Once the cigarettes reach the EW, they transfer from the manufacturer's bond to the EW's bond. The EW is now liable for the tax until proof of exportation is submitted or the cigarettes are transferred to another EW's bond.

Cigarettes may also be exported through an FTZ or CBW. Upon entry into the FTZ or CBW the cigarettes are considered to be exported. FTZs and CBWs are under Customs jurisdiction, however ATF may gain access to them with coordination through Customs.

DOMESTIC CIGARETTES

20 CIGARETTES = 1 PACK
25 CIGARETTES = 1 PACK

10 PACKS = 1 CARTON
8 PACKS = 1 CARTON

200 CIGARETTES = 1 CARTON

12,000 CIGARETTES = 1 CASE (12M)* 60 CARTONS = 1 CASE
6,000 CIGARETTES = ½ CASE (6M)

60,000 CIGARETTES = 5/10 THOUSAND STD CASES
6/12 THOUSAND STD CASES
3,000 PACKS
300 CARTONS

EXPORT CIGARETTES

10,000 CIGARETTES = 1 CASE (10M)
5,000 CIGARETTES = ½ CASE (5M)

* 12M/6M or 10M/5M notes markings of how many cigarettes there are per case. However, a case marked 12M/6M or 10M/5M will not necessarily contain 12,000/6,000 or 10,000/5,000 cigarettes, since the cases may be broken up. Individual cartons should be visually verified.

The 5 states that do not tax stamp their cartons are: *Alaska, Hawaii, Michigan, North Carolina and South Carolina.*

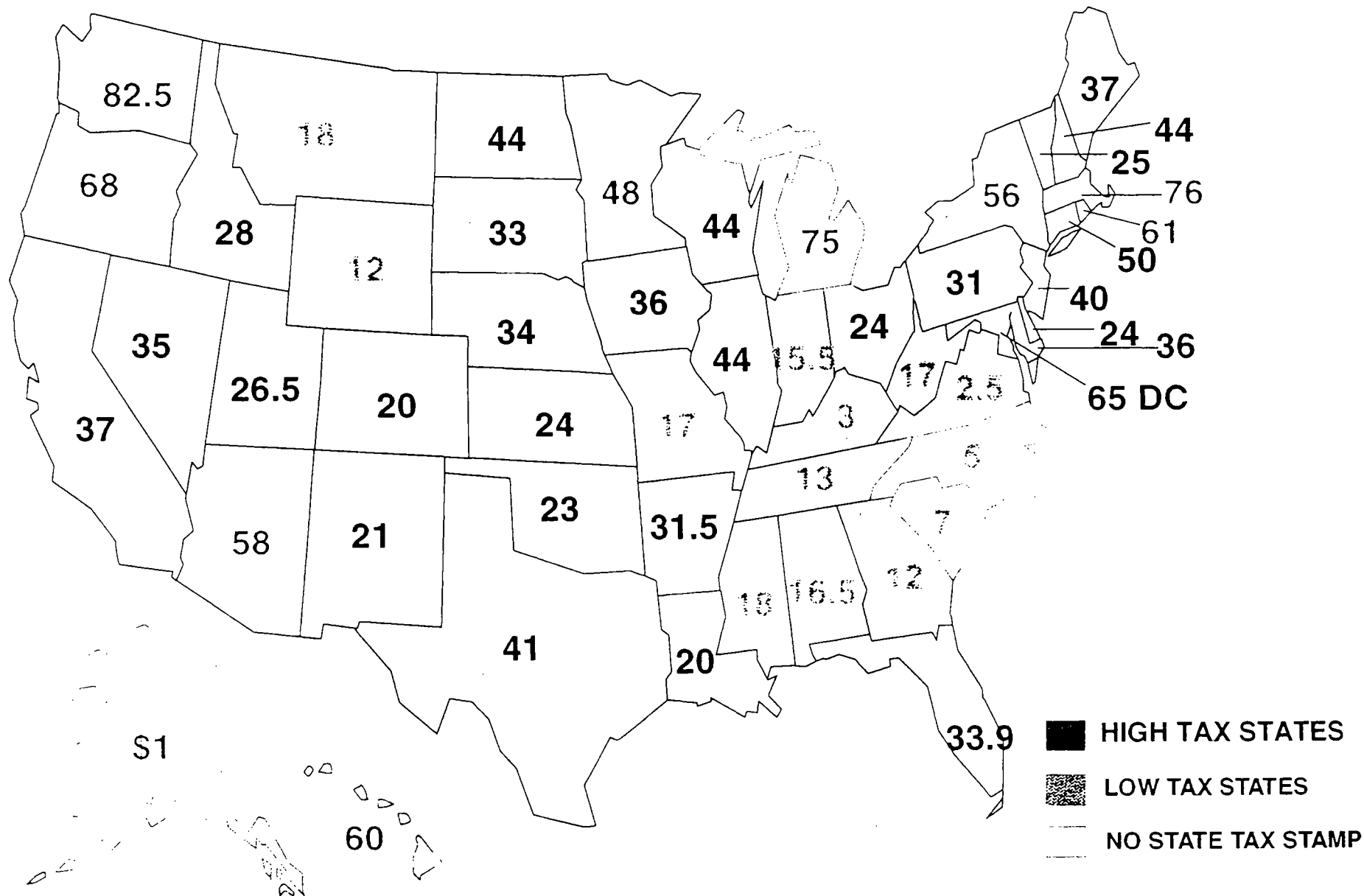
FEDERAL TAX

\$12.00 per 1,000 cigarettes
\$00.24 per pack of 20 cigarettes
\$00.30 per pack of 25 cigarettes

At Least 60,000+ Cigarettes Are Needed for an ATF Criminal Case.

STATE EXCISE TAX RATE ON CIGARETTES

20 CIGARETTE PACK/ IN CENTS



DISTILLED SPIRITS

Federal Tax Rate = \$13.50 per proof gallon

Equivalents of Commonly Diverted Case Sizes

<u>Bottle size</u>	<u>Bottles per case</u>	<u>Liters per case</u>	<u>Proof</u>	<u>Tax Rate/bottle</u>	<u>Tax Rate/case</u>
1 liter	12	12.0	80	\$2.85	\$34.20
1.75 liter	6	10.5	80	\$4.99	\$29.90

DISTILLED SPIRITS

Federal Tax Rate = \$13.50 per proof gallon

Equivalents of Commonly Diverted Case Sizes

<u>Bottle size</u>	<u>Bottles per case</u>	<u>Liters per case</u>	<u>Proof</u>	<u>Tax Rate/bottle</u>	<u>Tax Rate/case</u>
1 liter	12	12.0	80	\$2.85	\$34.20
1.75 liter	6	10.5	80	\$4.99	\$29.90

State Liquor Excise Tax Rates

January 1, 1997

STATE	EXCISE TAX RATES		
	SALES TAXES (\$ per gallon)	APPLIED	OTHER TAXES
Alabama	see footnote (1)	Yes	
Alaska	\$5.60	n.a.	under 21% - \$0.85/gallon
Arizona	3.00	Yes	
Arkansas	2.50	Yes	under 5% - \$0.50/gallon. under 21% - \$1.00/gallon: \$0.20/case and 3% off- 14% on-premise retail taxes
California	3.30	Yes	over 50% - \$6.60/gallon
Colorado	2.28	Yes	
Connecticut	4.50	Yes	under 7% - \$2.05/gallon
Delaware	3.75	n.a.	under 25% - \$2.50/gallon
Florida	6.50	Yes	under 17.259% - \$2.25/gallon. over 55.780% - \$9.53/gallon \$0.10/ounce on-premise retail tax
Georgia	3.79	Yes	\$0.83/gallon local tax
Hawaii	5.87	Yes	
Idaho	see footnote (1)	Yes	
Illinois	2.00	Yes	under 14% - \$0.23/gallon: \$0.50/gallon in Chicago and \$1.00/gallon in Cook County
Indiana	2.68	Yes	under 15% - \$0.47/gallon
Iowa	see footnote (1)	Yes	
Kansas	2.50	no	8% off- and 10% on-premise retail tax
Kentucky	1.92	Yes*	under 6% - \$0.25/gallon: \$0.05/case and 9% wholesale tax
Louisiana	2.50	Yes	under 6% - \$0.32/gallon
Maine	see footnote (1)	Yes	
Maryland	1.50	Yes	
Massachusetts	4.05	Yes*	under 15% - \$1.10/gallon. over 50% alcohol - \$4.05/proof gallon: 0.57% on private club sales
Michigan	see footnote (1)	Yes	
Minnesota	5.03	--	\$0.01/bottle (except miniatures) and 8.5% sales tax
Mississippi	see footnote (1)	Yes	
Missouri	2.00	Yes	
Montana	see footnote (1)	n.a.	
Nebraska	3.00	Yes	

Nevada	2.05	Yes	under 14% - \$0.40/gallon and under 21% - \$0.75/gallon.
New Hampshire	see footnote (1)	n.a.	
New Jersey	4.40	Yes	
New Mexico	6.06	Yes	
New York	6.44	Yes	under 24% - \$2.54/gallon; \$1.00/gallon New York City
North Carolina	see footnote (1)	Yes*	
North Dakota	2.50	--	7% state sales tax
Ohio	see footnote (1)	Yes	
Oklahoma	5.56	Yes	\$1.00/bottle on-premise and 12% on-premise
Oregon	see footnote (1)	n.a.	
Pennsylvania	see footnote (1)	Yes	
Rhode Island	3.75	Yes	
South Carolina	2.72	Yes	\$5.36/case and 9% surtax
South Dakota	3.93	Yes	under 14% - \$0.93/gallon, 2% wholesale tax
Tennessee	4.00	Yes	\$0.15/case and 15% on-premise; under 7% - \$1.10/gallon.
Texas	2.40	Yes	14% on-premise and \$0.05/drink on airline sales
Utah	see footnote (1)	Yes	
Vermont	see footnote (1)	no	
Virginia	see footnote (1)	Yes	
Washington	see footnote (1)	Yes*	
West Virginia	see footnote (1)	Yes	
Wisconsin	3.25	Yes	
Wyoming	see footnote (1)	Yes	
Dist. of Columbia	1.50	Yes	8% off- and 9% on-premise sales tax
U.S. Median	\$3.25		

Source: Compiled by FTA from various sources.

* Sales tax is applied to on-premise sales only.

(1) In 18 states, the government directly controls the sales of distilled spirits. Revenue in these states is generated from various taxes, fees and net liquor profits.

EXISTING CONTROLS FOR THE ALCOHOL & TOBACCO INDUSTRIES UNDER CURRENT LAW

ALCOHOL

TYPE OF INDUSTRY	DISTILLED SPIRITS PLANT	WHOLESALER AND/OR IMPORTER	RETAILER
DOCUMENTS REQUIRED:			
APPLICATION - FAA	YES	YES	NO
APPLICATION - IRC	YES	NO	NO
BOND(S)	YES	NO	NO
CORPORATE CHARTER OR CERTIFICATE	YES	YES	NO
LIST OF OFFICERS AND DIRECTORS	YES	YES	NO
PERSONNEL QUESTIONNAIRES	YES	YES	NO
LIST OF PERSONS HOLDING MORE THAN 10% STOCK	YES	YES	NO
TRADE NAME REGISTRATION	YES	YES	NO
APPLICANT RECEIVES:			
BASIC PERMIT - FAA	YES*	YES	NO
IRC PERMIT	YES*	NO	NO
APPROVED REGISTRATION	YES	NO	NO
STATE LICENSE/PERMIT	YES	YES	YES
SPECIAL OCCUPATIONAL TAX (SOT)	YES	YES	YES
RECORDS:			
MONTHLY REPORT OF OPERATIONS	YES	NO	NO
RECORDS OF RECEIPT	YES	YES	YES
RECORDS OF DISPOSITION	YES	YES	YES***

TOBACCO

TOBACCO PRODUCTS MANUFACTURER	EXPORT WAREHOUSE PROPRIETOR	WHOLESALER AND/OR IMPORTER**	RETAILER
N/A	N/A	N/A	N/A
YES	YES	NO	NO
YES	YES	NO	NO
YES	YES	NO	NO
YES	YES	NO	NO
YES	YES	NO	NO
YES	YES	NO	NO
YES	YES	NO	NO
N/A	N/A	N/A	N/A
YES	YES	NO	NO
NO	NO	NO	NO
YES	YES	YES	YES
YES	YES	NO	NO
YES	YES	NO	NO
YES	YES	NO	NO
YES	YES	YES***	YES***

* DEPENDING UPON PROPOSED ACTIVITIES

** WILL NEED AN IMPORTER'S PERMIT BY YEAR 2000

*** IF MORE THAN 20 WINE GALLONS FOR ALCOHOL/ MORE THAN 60,000 CIGARETTES FOR TOBACCO

- a. reasonably foreseeable
- b. in furtherance of
- c. original conspiracy
- d. committed while the person is a part of the conspiracy

18 U.S.C. § 1001

False statements in matters within jurisdiction of any department or agency of U.S.

IRC TAX VIOLATIONS ON NON-UNITED STATES TAX PAID LIQUOR

26 U.S.C. § 5601(a)
(1) - (a) (15)

Penalties for unlawful warehousing, processing, withdrawal distilling purchase of distilled spirits, etc. include up to 5 years imprisonment and/or \$10,000 fine

26 U.S.C. § 5602

Penalties for tax fraud by distiller-Up to 5 years imprisonment and/or \$10,000 fine

26 U.S.C. § 5603

Penalties for fraudulent violations of IRC recordkeeping requirements-up to 5 years imprisonment or \$10,000 fine

26 U.S.C. § 5691(a)
Willful failure to pay
special occupational tax
as a wholesaler.
Punishable by up to 2
years in prison

26 U.S.C. § 7201
Willful intent to evade
or defeat tax. Penalty-
Up to 5 years
imprisonment/fine up to
\$100,000 (\$500,000 fine
if corporation

26 U.S.C. § 7206
Fraud and false statements

Penalty-Up to 3 years
imprisonment and/or
\$100,000 fine. \$500,000
fine in the case of a
corporation

26 U.S.C. § 5762

Criminal penalties
associated with failing
to comply with Internal
Revenue law relating to
taxes, records and
permits for manufacturers
and exporters of tobacco
products

18 U.S.C. § 1263

Anyone who ships distilled spirits
in United States must have a bill
of lading accompanying shipment
accurately showing contents of
shipment and consignee.

IV. Regulatory Issues
Alcohol/Diversion

A. Tax Cases

Distilleries must document the exportation of liquors.

ATF's position set forth in Industry Circular 94-1 dated 4/14/94.

26 U.S.C. § 5001 imposes tax on all distilled spirits.

26 U.S.C. § 5111 requires wholesalers to pay \$500/yr. special (occupational) tax. The penalty for willful failure to pay SOT is \$5,000/2 yrs.

26 U.S.C. § 5214(a)(4) allows distilled spirits to be removed without payment of tax after filing bonds required by 26 U.S.C. § 5175 and complying with ATF regulations.

26 U.S.C. § 5005, proprietor is liable for tax of spirits produced on the bonded premises of DSP.

Relief from liability only occurs when export occurs pursuant to 26 U.S.C. § 5005(e) and distillery provides proof of export. ATF regulations specify certain proof of export. See 27 C.F.R. §§ 252.40 and 252.250-269.

B. Documenting Alcohol Diversion
Tax Cases

1. Establish that the proof of export is inadequate
2. Establish false bills of lading or false ATF Form 5100.11

C. Administrative Liability
(Tax Paid Alcohol Cases)

Establish violation of conditions of basic permit (violation of 27 U.S.C. § 204(d)) due to:

1. 18 U.S.C. § 1154(a) and 1156 illegal shipments of liquor and/or illegal possession into Indian Country.
(Discussed in detail in Indian section)

2. Shipments of distilled spirits into state in violation of State law is a violation of Webb-Kenyon statute, 27 U.S.C. § 122, as well as 21st Amendment.

3. ATF Industry Circular 1995-1 (1/19/95) discusses liability as principal or aider and abettor for violations of Internal Revenue Code, FAA Act, Webb-Kenyon, and Indian provisions

VI. State and Local Law Issues

The Webb-Kenyon Act, 27 U.S.C. § 122, a statutory declaration of the twenty-first amendment, provides that the shipment of alcoholic beverages from one State into any other State in violation of the laws of the receiving State is prohibited.

Neither the twenty-first amendment nor Webb-Kenyon provide for any criminal or civil penalties for violations thereof.

The Federal Alcohol Administration Act (FAA Act), 27 U.S.C.

§ 203, requires a basic permit in order to engage in the business of importing alcoholic beverages, distilling distilled spirits or producing wine. Finally, persons who engage in the business of purchasing for resale at wholesale distilled spirits, wine, or malt beverages must obtain basic permits.

27 U.S.C. § 204(d) provides that basic permits are conditioned upon compliance with the twenty-first amendment and the laws relating to its enforcement. As such, violation of either the twenty-first amendment or Webb-Kenyon arising from violations of State law either directly or as an aider or abettor could result in the suspension or revocation of the basic permit of the violator.

VIII. Tobacco Diversion and Regulatory Requirements

Introduction

Criminals engage in tobacco diversion for the same reason as alcohol diversion. They make profits by transporting cigarettes from low tax jurisdictions to high tax jurisdictions and from regulated channels to unregulated channels.

Cigarettes are diverted from low tax jurisdictions like North Carolina and Virginia to high tax jurisdictions like New York, Michigan, Washington, and from the U.S. to Canada.

Cigarettes are diverted from alleged export to the U.S. market by filing false paperwork at FTZ's, CBW's, and export warehouses, wherein goods are allegedly exported but in fact stay in the United States. Cigarettes are smuggled into the United States from other countries, including Canada and Mexico.

A. CONTRABAND CIGARETTE
TRAFFICKING ACT (CCTA) (18 U.S.C. §
2341 et seq.)

Makes it unlawful for any person to ship, transport, receive, possess, sell, distribute or purchase in excess of 60,000 cigarettes which bear no evidence of State tax payment in State in which cigarettes are

found, if such State requires a stamp to evidence payment of taxes.

Elements of CCTA Act violation

1. Defendant shipped, transported, received, possessed, sold, distributed or purchased cigarettes without the requisite tax stamps;
2. Quantity of cigarettes exceeded 60,000 cigarettes, i.e. more than 5 cases of cigarettes
3. The State required a tax stamp.
4. CCTA applies to shipments over 5 cases. United States v. DiMaria, 727 F.2d 265 (2nd Cir. 1984). 60,000 cigarettes must be transported to fall within scope of CCTA. U.S. v. Paradiso, 689 F.2d 28 (2nd Cir. 1982).

Penalties-Up to 30 years imprisonment or fines.

5. ATF takes the position that the Contraband Cigarette Act applies to Indian tribes. CC Case No. 41,112, 10/9/92. U.S. v. Baker, 63 F.3d 1478 (9th Cir. 1995), cert. denied 116 S.Ct. 824 (1996) (Indians are not exempt from CCTA and Washington State tax is valid to Indians); U.S. v. Gord, 77 F.3d 1192 (9th Cir. 1996) (Unstamped cigarettes which were not pre-approved by Washington State Dept. of Revenue for resale to Indians were contraband under CCTA even if smokeshop were tribal organization and distributes cigarettes to only Native Americans).

6. While the regulations do not preclude a distributor from dividing a single agreement for the disposition of more than 60,000 cigarettes or less, the distributor must record the required information for each component of the agreement. T.D. ATF-73, 45 Fed. Reg. 18609, July 21, 1980. A distributor who fails to keep the required records for each component of an agreement for the disposition of more than 60,000 cigarettes would be in violation of the regulations.

Thus, even where a defendant does not have actual possession of more than 60,000 cigarettes, it may be possible to establish that such defendant has constructive possession of such a quantity of cigarettes because such defendant has the power and intention at a given time to exercise dominion and control over the cigarettes, either directly or through others.

Given this stated purpose, any interpretation of the law that would categorically allow organized crime and large scale operators to circumvent its scope by merely splitting shipments would allow such persons to operate with virtual impunity, a situation which cannot be tolerated. See Id. at 5524.

9. CCTA can be used in conjunction with wire, mail fraud, money laundering, and RICO statutes. U.S. v. Baker (Paragraph 5) (CCTA violation resulted in RICO case and million dollar forfeiture using the aforementioned statutes)

B. JENKINS ACT (15 U.S.C. § 375)
Any person who sells cigarettes in interstate commerce when the cigarettes are transported into a State taxing their sale to other than a licensed distributor must:
(1) first file w/State tobacco tax administrator their name and place of business and (2) by the 10th of each calendar month an invoice detailing shipments made into the State during the previous month including purchaser, brand, and quantity.

7. Where a distributor effects multiple agreements for the disposition of cigarettes which if executed singly would exceed 60,000 in quantity in order to avoid the purview of the regulations, a determination as to whether such distributor is nevertheless covered by the regulations must be made upon the facts of the particular case. As stated in T.D. ATF-73, it is impossible to provide a general statement or definition as to what constitutes evidence of a distributor's intent to avoid the requirements of this regulation outside the context of a particular case. 45 Fed. Reg. 18612.

8. Similarly, it is not possible to provide a general statement as to whether a person is in violation of section 2342(a) where such person divides quantities of more than 60,000 cigarettes into smaller components in order to avoid the purview of the law. However, since the term contraband cigarettes is defined to require "possession" of greater than 60,000 cigarettes, it may be possible to establish a violation of section 2342 under the doctrine of constructive possession, depending upon the facts of a particular case.

CIGARETTE HOTLINE INTAKE REPORT

HOTLINE NUMBER 97- 1-800-659-6242

CALLER'S NAME: _____
PHONE NUMBER: _____
ORGANIZATION: _____
POSITION: _____

INCIDENT DATA

INCIDENT: _____

DATE: _____ TIME: _____
LOCATION: _____
DESCRIPTION: _____

AMOUNT: _____
PRINTED CODING/MARKINGS/OTHER IDENTIFICATION: _____

CONTAINER/TRAILER NUMBERS: _____

OTHER: _____

INDIVIDUAL OR BUSINESS IN POSSESSION: _____

ADDRESS OF POSSESSOR: _____

IF KNOWN, ORIGINAL SOURCE OF CIGARETTES: _____
CIRCUMSTANCES: _____

HAS ATF LAW ENFORCEMENT BEEN NOTIFIED? _____(Y) _____(N)

WERE OTHER AGENCIES NOTIFIED? _____(Y) _____(N)

AGENCY: _____

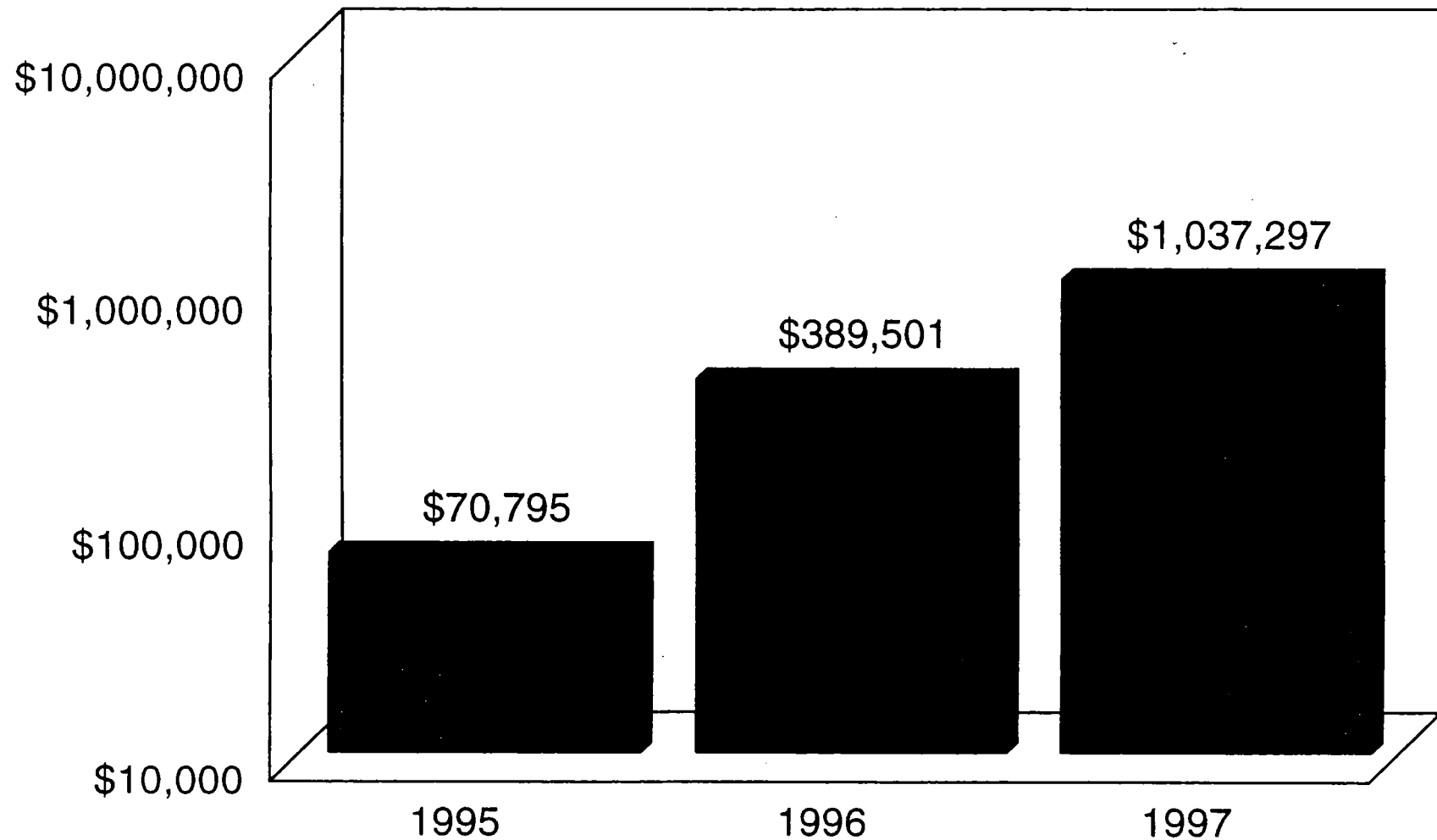
AGENCY REPORT NUMBER: _____

AGENT/INSPECTOR'S NAME: _____

TAKEN BY: _____ TIME: _____

TOBACCO SEIZURES IN DOLLARS

FROM FY 1995-1997



VIOLATIONS

IRC

FAA

**COMMERCE WITH
NATIVE
AMERICANS**

**MONEY
LAUNDERING
CONSPIRACY**



VIOLATIONS



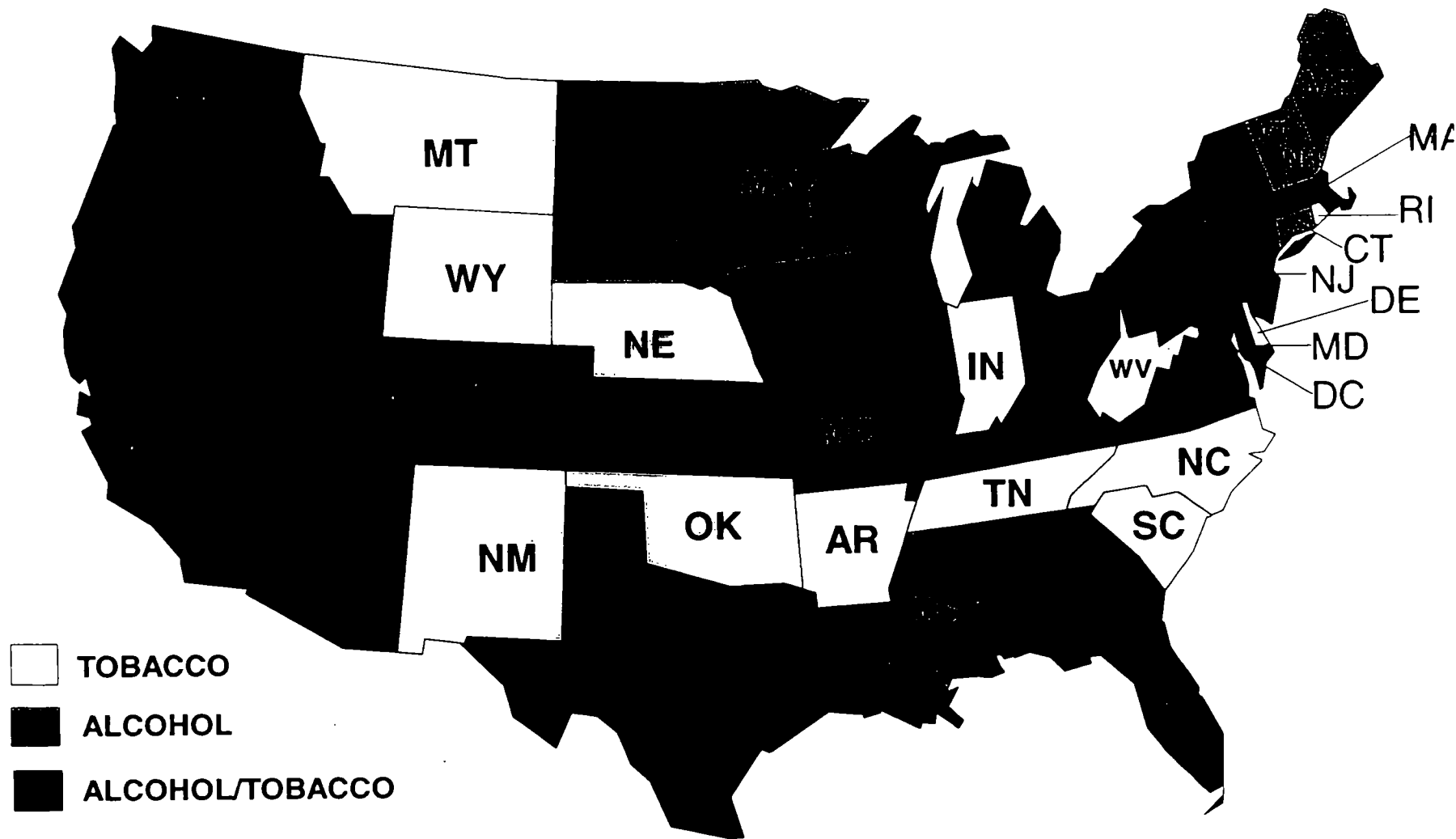
ITAR

CCTA

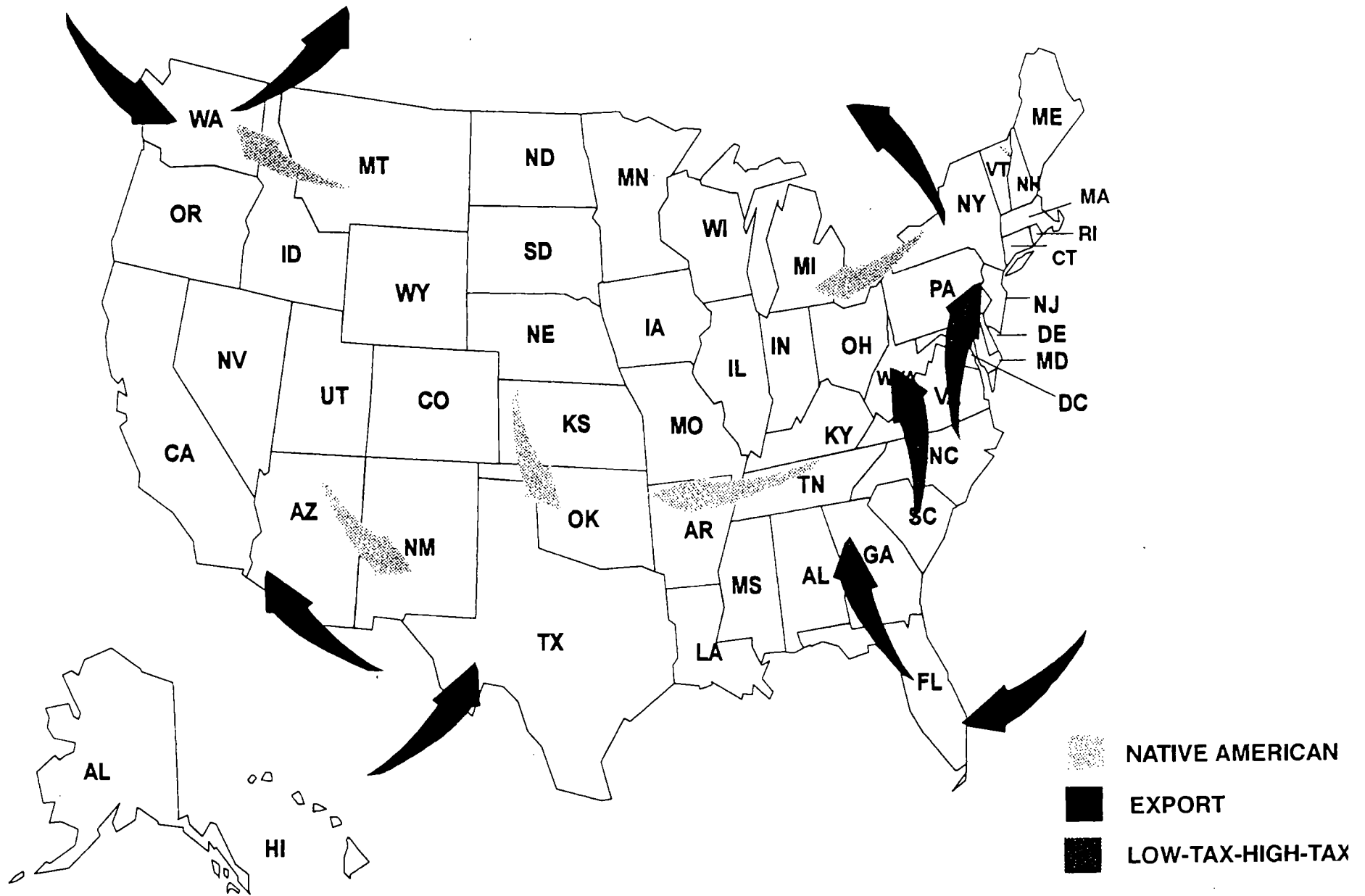
RICO

**WIRE/MAIL
FRAUD**

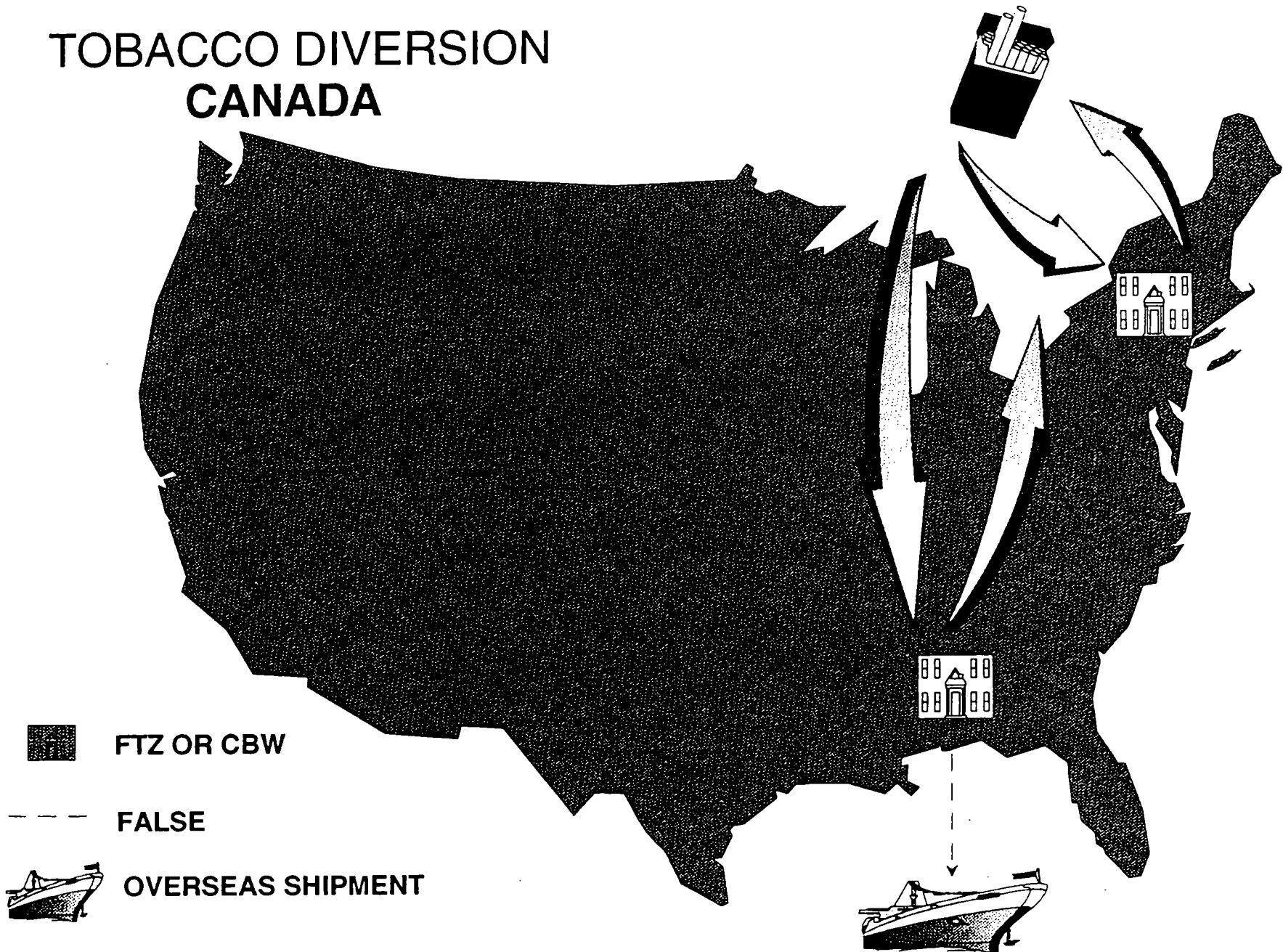
**STATES WITH A&T DIVERSION & CONTRABAND ACTIVITIES
1993-1997**



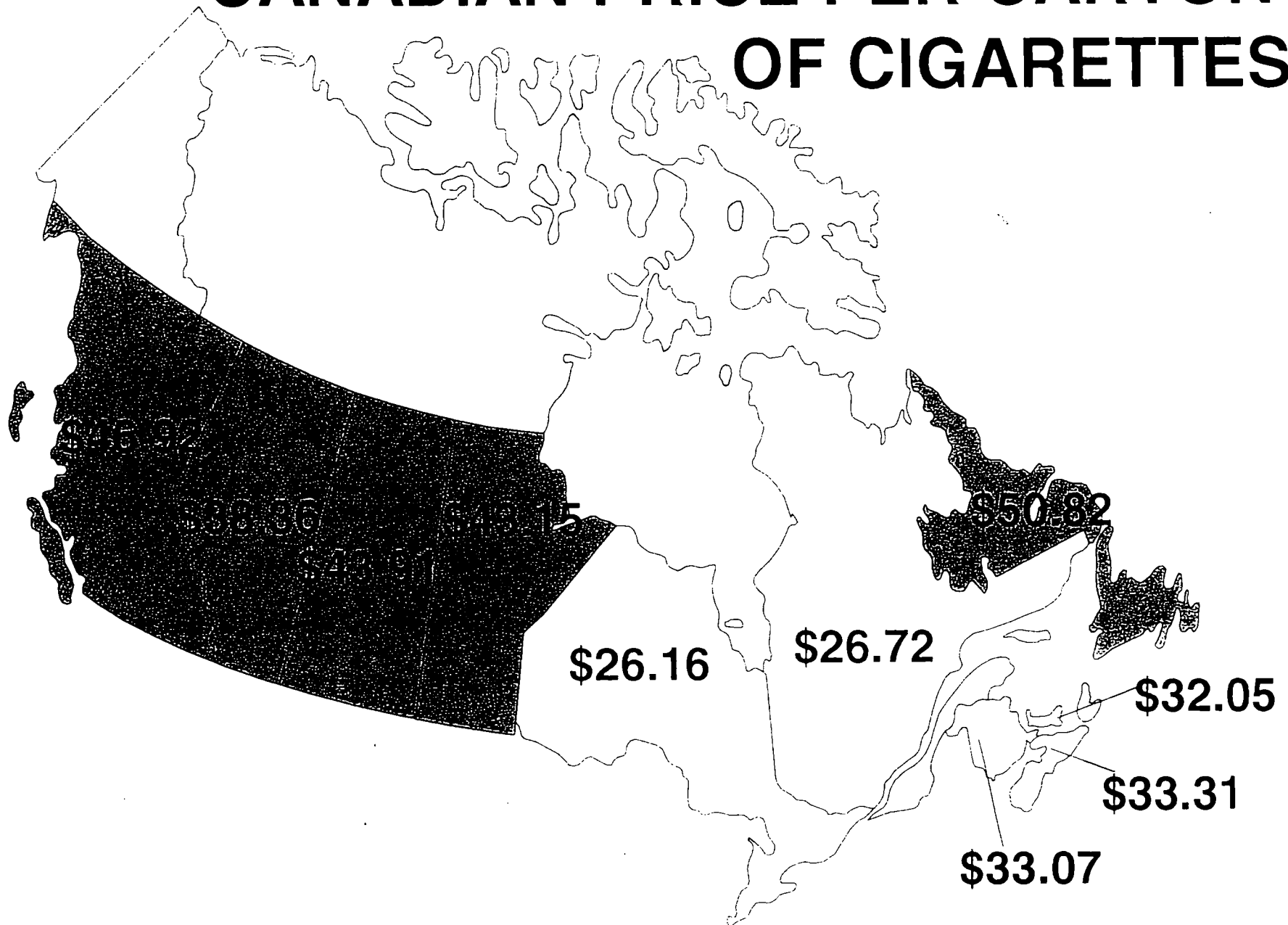
U.S. DIVERSION & CONTRABAND TRAFFICKING ACTIVITY



TOBACCO DIVERSION CANADA



CANADIAN PRICE PER CARTON OF CIGARETTES



MICHIGAN

EST \$50 M PER YEAR LOSS

4TH HIGHEST STATE TAX

NO TAX STAMP ON PACKS

**INVOLVES MAINLY MIDDLE
EASTERN OC**

OBTAIN CIGARETTES FROM

LOW TAX STATES

NY INDIAN RESERVATIONS

WASHINGTON

- LOSES APPROX \$100 M PER YEAR**
- 2ND HIGHEST STATE CIGARETTE TAX**
- NON-COMPLIANCE**
 - 60% FROM WA INDIAN RESERVATIONS**
 - 11% FROM MILITARY BASES**
 - 29% FROM CROSS BORDER SHOPPERS, MAIL ORDER AND EXPORT SCHEMES**

CALIFORNIA

- LOSES APPROX \$30 M PER YEAR
- SOURCE IS PRIMARILY "EXPORTS" TO MEXICO
- MAIN BLACK MARKET SITE IS IN LA
- INVOLVES DIFFERENT CRIMINAL GROUPS

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The Detroit News

July 22, 1997, Tuesday

SECTION: Business; Pg. Pg. B1

LENGTH: 558 words

HEADLINE: Cigarette taxes force smokers to cross borders in search of deals

BYLINE: By Kathy Kristof

BODY:

When Michigan hiked its cigarette excise tax by 50 cents to 75 cents per pack in 1994, taxable cigarette sales plunged 21 percent. But, sales in neighboring Indiana rose 8.5 percent.

California, MASSACHUSETTS, Michigan and New York, with combined populations of 65.4 million and an average cigarette excise tax of 55 cents per pack, reported fewer taxable cigarette sales than the states of Indiana, Kentucky, Missouri, New Hampshire, North Carolina, Tennessee and Virginia, which host half the population and average excise taxes of just 12 cents.

New Hampshire sold twice as many packs of cigarettes as MASSACHUSETTS, even though the rate of smoking in both states is nearly identical. The difference: MASSACHUSETTS has a 76-cent per-pack excise tax, while New Hampshire's excise tax is just 25 cents per pack.

Facts like that amount to a guilty little secret for people like Warren. Once every few weeks, the Washington, D.C., native zips across the Virginia border and loads up on cigarettes. Because cigarette taxes amount to 65 cents per pack in D.C., but less than 3 cents a package in Virginia, he can buy three packs for the price of two.

With a pack-a-day habit -- and a host of chain-smoking friends -- Warren's modest bout into the world of cigarette smuggling saves him a small fortune.

He's not alone. The growing disparity in state cigarette excise tax rates has led to a dramatic increase in both large-scale interstate smuggling and simple "cross-border sales" like Warren's. Although it is not illegal to buy cigarettes

in Virginia and smoke them elsewhere, smuggling for profit is. Moreover, some states limit the number of excise taxable items that come in. Warren asked that his name not be used in print because he doesn't want to explain his trunk full of smokes if is ever stopped by the authorities.

"I don't think I'm actually breaking the law," he says. "But I may be stretching it."

Cross-border cigarette shopping soared 395 percent between 1980 and 1994 as the state-by-state disparity in cigarette excise taxes widened, according to the Tax Foundation, a Washington, D.C.-based tax research organization. Full-scale cigarette smuggling -- the type done for profit with semi-trucks -- rose a tidy 253 percent during the same period, according to the tax research group.

While tax rates on cigarettes have varied for years, these differences have widened substantially in the past several years and appear to be widening even still. That's mainly because when state budgets began to get squeezed earlier this decade, a host of states opted to boost their revenues by taxing "sin."

Or, at least, unpopular habits, like smoking, drinking and driving a lot. As a result, excise taxes on cigarettes began to soar in some states, where in other states where tobacco lobbies were stronger, they held pat.

Meanwhile, Indian reservations, where Native American tribes are able to sell goods tax-free, have become a haven for mid-state smokers in high-tax states. In Washington, for example, cigarette sales on reservations are believed to account for 14 percent of all cigarettes sold in the state.

Syndicated columnist Kathy Kristof appears regularly in The Detroit News Business section. Contact her through the Internet at kristof@news.latimes.com. Distributed by Los Angeles Times Syndicate.

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Thursday, April 24, 1997



Multistate probe of contraband yields indictments *Cigarettes were trucked to New York*

BY TOM CAMPBELL
Times-Dispatch Staff Writer

A federal and state crackdown on a cigarette-smuggling operation that cheated Virginia and three other states out of \$18 million in tobacco and sales taxes has produced 30 federal indictments, U.S. prosecutors announced yesterday.

The investigation that grew into a multistate, multiagency investigation of the smuggling of cigarettes out of Virginia is expected to produce at least 30 more indictments.

Helen F. Fahey, U.S. attorney for Eastern Virginia, and law enforcement officials from Virginia, New York, Maryland and Pennsylvania announced "Operation Butt-Out" in a news conference yesterday.

The indictments include individuals as well as corporations formed specifically to gain wholesale licenses to obtain the cigarettes to smuggle, authorities said.

Smugglers typically buy cigarettes wholesale at Virginia outlets -- including Sam's Club and Price Club -- drive them to New York City without paying taxes and sell them to buyers there. The Virginia wholesalers do nothing illegal by making such sales, authorities said. They have cooperated fully in the investigation.

"Virginia being a tobacco state and a low-tax state is what makes it attractive," said Bruce Knowlton of the Virginia Alcoholic Beverage Control Board investigations unit.

ABC is part of the 2-year-old smuggling investigation because some of the early targets of the probe held ABC licenses, said Anne Petera, chairman of the ABC Board.

According to law enforcement estimates, smugglers pay an average of \$12.29 per carton in Virginia and typically buy a truckload of about 1,000 cartons per run. They sell them at \$16 a carton to a New York connection for a profit of \$3,710.

The connection sells them, through small stores or bars, for \$21.50 -- still less than the legitimate New York price for cigarettes, with all taxes paid. The connection makes about \$5,500 per truckload.

"The average smuggler will do three loads a week," Knowlton said. He said 10 to 15 smugglers have been operating in and out of Virginia during a typical week, and sometimes that many per day.

Knowlton said the estimated yearly loss in tax revenue from Virginia-to-New York City cigarette smuggling operations is \$16.27 million.

That's about \$1.3 million to Virginia, about \$13 million to New York State and about \$1.8 million to New York City, which imposes its own cigarette tax on top of the state's tax.

"The biggest loser is the state of New York," Knowlton said.

Robert L. Shepherd, deputy commissioner of the New York State Office of Tax Enforcement, attended the news conference.

"It's a multimillion dollar problem," Shepherd said. "And it's mostly our problem, but it's refreshing to see all the agencies involved, state and federal, working so effectively together."

Many of those indicted so far are recent immigrants from the Middle East and Asia, with connections in New York but living in Virginia.

Sometimes only customers known to the retailer get the smuggled cartons, which carry counterfeit tax stamps or none at all. Sometimes they sell to anyone.

"Sometimes the customers know they've gotten bootleg cigarettes," Shepherd said. "Sometimes they don't. Sometimes they don't care."

Assistant U.S. Attorney David Schiller of the Richmond office said the list of indictments covers six conspiracy groups and a few individuals.

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Glossary

Broker - A person who negotiates contracts of purchase and sale.

Carrier - Any person, company, corporation, or organization including a proprietor, owner, consignor, or consignee who transports distilled spirits, denatured spirits, or wine in any manner for himself or others.

Customs Bonded Warehouse (CBW): A building or other secured area under Customs' control in which dutiable goods for export or import may be stored, manipulated, or undergo manufacturing operations without payment of duty. Goods can only move between two CBW's; more than two movements among CBW's requires that the duty be paid.

Consignee - Person to whom goods have been transferred or shipped.

Consignor - The person transferring goods.

Contraband Cigarettes (CCTA)- The possession, transportation, receipt, or shipment of any quantity of cigarettes in excess of 60,000 not bearing the required tax indication of the State in which they are found is prohibited. Tobacco manufacturers, tobacco exporters, common carriers transporting cigarettes under bills of lading and State stamping agents are exempt.

DAG-71 - A Department of Justice form utilized to request a share of property Federally forfeited by a Justice agency (i.e., FBI, DEA, INS). Any Federal, State, or local law enforcement agency that directly participates in an investigation or prosecution that results in a Federal forfeiture may request an equitable share of the net proceeds of the forfeiture.

Detention - Process which enables alcohol products to be held pending determination of tax status.

Distilled Spirits Plant (DSP) - an establishment qualified for distilling, warehousing, processing or any combination thereof.

Diversion - the rerouting of a good or commodity from a legal course to an illegal course.

Electronic fund transfer (EFT): Any transfer of funds effected by a person's financial institution.

Export Warehouse (EW): A bonded internal revenue warehouse for the storage of tobacco products and cigarette papers and tubes, upon which internal revenue tax has not been paid, for subsequent shipment to a foreign country, or for consumption beyond the jurisdiction of the internal revenue laws of the United States.

FAA ACT - The Federal Alcohol Administration Act is the law which provides for the issuance of basic permits to distillers, wholesalers and importers.

Freight Forwarder - A person who arranges the best price, by air, truck, rail or ocean for their client's export shipments.

Foreign Trade Zone (FTZ) - Also known as **Free Trade Zone**. A defined area, outside the Customs territory of the United States, where operations involving foreign and domestic merchandise can take place without being subject (under certain circumstances) to the US customs laws or the payment of duty or tax. Merchandise may be exported, imported, destroyed, or sent into Customs territory from the zone. Cargo can be shuffled among FTZ's until export.

Importer - Any person who brings distilled spirits, wine, beer or tobacco products into the United States.

Internal Revenue Code (IRC) - Contains the Federal laws governing the production and taxation of alcohol and tobacco products.

Non Vessel Operating Commercial Carrier (NVOCC) - leased space available for exported commodities on a passenger ship or steamship line. Potential means of diversion in that the NVOCC can reroute cargo, manipulate cargo or substitute cargo on the dock without the knowledge or consent of DSP, manufacturer or freight forwarder. The cargo container could then still show up as loaded aboard the line.

Retail Liquor Dealer (RLD) - Any person who sells or offers for sale distilled spirits, wine, or beer to any person other than a dealer.

Special Occupational Tax (SOT) also referred to as **Special Tax** - A special tax is imposed by the Internal Revenue Code on persons engaged in certain trades or businesses. Such business includes distilled spirits plants, importers, wholesalers, retail liquor dealers, manufacturers of tobacco products and export warehouses.

Tax determined - Term means that taxable quantities of articles subject to tax have been established.

Tax Free - Term refers to the exemption of Federal taxes on commodities to be exported. Also refers to commodities, such as alcohol and tobacco, that is used for consumption on international shipping vessels.

Tax paid - Term means that all applicable taxes imposed by law have been determined or paid as provided by law.

TD F 92-22-46 - A Department of Treasury form utilized to request a share of property Federally forfeited by a Treasury agency (i.e., US Customs, IRS, ATF or U.S. Secret Service). Any Federal, State, or local law enforcement agency, as well as foreign countries, that directly or indirectly participated in an investigation or prosecution that results in a Federal forfeiture by a Treasury agency may request an equitable share of the net proceeds of the forfeiture. Similar in function to the Department of Justice form, **DAG-71**.

Trafficking - to carry on, trade or deal in the illegal trade of a commodity. Under the CCTA this includes the movement of goods illegally across state lines.

Wholesale liquor dealer: A person who sells or offers for sale distilled spirits, wine or beer to another dealer. A retailer who sales more than 20 gallons of liquor at one time, under Federal law, acts as a wholesaler.

Tax Report

A Special Summary and Forecast Of Federal and State Tax Developments

ROCK STARS TANGLE with the IRS over deducting wild onstage clothing.

Musicians and singers often wear unusual clothes during performances, but does their garb qualify as an ordinary and necessary business expense? This was one of several taxing questions in a case involving Stevie Nicks of the legendary group Fleetwood Mac. She said her flowing onstage attire "is not suitable for ordinary wear." She adds that much of it is discarded after concerts because it "simply cannot be reused, given the energy levels" of her performances and "the heat generated on stage from lights and physical exertion."

George G. Short, a California lawyer, says a "tentative settlement" has been reached with the IRS on this and other issues, such as deductions for a home office and a personal manager. He declines to elaborate, and the IRS says it can't comment. In a separate case, the Tax Court recently allowed a musician touring with Rod Stewart to deduct only \$200 of \$695 in "stage clothes," holding that most of the items were "adaptable for general and personal wear."

The judge rejected any deduction for the man's underwear.

THE TAX BURDEN grows heavier for many families, a report says.

Despite all the talk about cutting taxes, the median-income family's total federal, state and local tax burden rose again this year, says the Tax Foundation, a nonprofit research group in Washington. Senior economist Claire M. Hiltz cites two main factors: growth of federal payroll taxes and general increases in state and local taxes.

During 1997, total state and local taxes represented nearly 13% of the median family's income, the report says. That was a record and up from 11.5% in 1985. Individual federal payroll taxes, which pay for such programs as Social Security and Medicare, totaled 7.3% of median family income, well above the 2% level in the mid-1960s.

A POPULAR TAX BREAK survives Congress's ax.

Congressional efforts failed once again this year to repeal the "14-day rule." This provision allows people to rent their residence for 14 days, or less, each year without owing any income taxes on the rent. This rule applies no matter how much rent is charged. Income from a rental for more than 14 days is fully taxable.

Advocates of repeal argued that the exclusion is unjustified, especially since there is no dollar limit, and that the revenue could be used for broader tax cuts. Congress's Joint Tax Committee estimated that repeal of the provision would raise about \$123 million over five years. Opponents of repeal included Rep. Charlie Norwood, a Georgia Republican whose district includes Augusta, home of the Masters golf tournament.

This provision also is very popular in sections of North Carolina that host furniture-industry conferences.

TAX-LAW COMPLEXITY angers many experts. The new law is "a slap in the face," says G. Fred Streuling, head of the tax-policy and simplification committee of the tax division of the American Institute of Certified Public Accountants. Mr. Streuling, also a Brigham Young University accounting professor, says "it's hard to understand" how lawmakers who only one year earlier were appealing for simplicity could have approved such a measure.

SLIGHTLY BEHIND SCHEDULE: A law enacted in 1996 required the Treasury to send a report to Congress by Jan. 31 this year on whether to recommend changes in the law on couples' joint tax liability. The Treasury said late yesterday it is "finalizing" the report.

BOOKS AND STUDIES proliferate on how to overhaul the tax system. The Senate Finance Committee plans to hold hearings on the subject next year. The General Accounting Office, a congressional investigative agency, will issue its own study early next year, says Lynda Willis, director of tax policy and administration issues.

PROBLEM-SOLVING SESSIONS at the IRS attract warm reviews.

This month, the IRS is holding its second round of problem-solving forums around the nation, where officials sit down with taxpayers in an effort to resolve disputes. Senate Finance Chairman William V. Roth Jr., who berated the IRS in September following disclosures of tax-collection abuses, praises the forums and says "many" people found last month's sessions helpful. The Delaware Republican will join IRS Commissioner Charles Rossotti today in Wilmington at a problem-solving session.

Although a few taxpayers complained of difficulties reaching the agency to get details of meetings, most reaction has been favorable. The IRS today will release results of a customer-service survey of more than 1,000 people who took part in the Nov. 15 event. The survey, developed and evaluated by an outside firm, shows the IRS got an overall rating of 6.46 on a scale of 1 to 7, with seven as the highest rating of "completely satisfied."

More than 75% of those responding gave the IRS the top rating of seven.

BRIEFS: Rep. Charles E. Schumer, a New York Democrat, introduces a bill that would let taxpayers get a receipt itemizing how the government spends their income-tax payment. . . . Still missing your 1996 federal income-tax refund check? Call 1-800-829-1040, an IRS official says. Nearly 100,000 refund checks were returned by the Postal Service as undeliverable.

—TOM HERMAN

THE WALL STREET JOURNAL
WEDNESDAY, DECEMBER 10, 1997

BR- Did you see this? Tom

Black market

Congress Warned of Black-Market Risk If It Boosts Cigarette Prices Too High

By JEFFREY TAYLOR

Staff Reporter of THE WALL STREET JOURNAL

WASHINGTON — In crafting tobacco legislation, Congress should avoid raising cigarette prices so much that a black market springs up to sell them more cheaply, law-enforcement officials told a House subcommittee.

The group, including representatives of the Royal Canadian Mounted Police and the U.S. Bureau of Alcohol, Tobacco and Firearms, testified that Canada's experience doubling cigarette prices from 1984 to 1993 held cautionary lessons for Congress as it considers steps to fight underage smoking. Smuggled cigarettes from the U.S. poured across the border, undercutting the goal of reducing tobacco consumption, the witnesses said.

"By early 1994, it was estimated as much as 40% of the Canadian domestic tobacco market was being supplied through smuggling," said Sgt. Alain Giroux of the Canadian Mounted Police. That led to an increase in violence associated with smuggling and in the involvement of organized crime.

The activity prompted a major crackdown on smuggling along the Canadian border by the Mounties and U.S. law-enforcement agencies, he said, plus a rollback of the cigarette-tax increases.

While public-health officials say price increases are the single most effective way to reduce teenage smoking, Republicans in Congress have frequently warned that a big increase or an attempt to ban ciga-

rettes would quickly result in a booming black market. The proposed \$368.5 billion national tobacco settlement that Congress is considering would provide a 62-cent per-pack price increase, which the industry contends will grow to more than \$1.50 a pack after retailer and wholesalers tack on their profit margins.

Yesterday's testimony before the Commerce Health and Environment subcommittee bolstered Republicans' argument, although Mr. Giroux noted that the border crackdown has allowed some Canadian provinces to begin increasing tobacco taxes without a corresponding increase in smuggling.

Moreover, a U.S. law-enforcement official testified that other components of the proposed settlement—including education, law-enforcement efforts and the lack of a sudden, dramatic price increase—might actually prevent development of a black market. "The resolution does not make the kind of drastic and immediate changes... that would almost certainly lead to... illegal markets," said Dennis C. Vacco, New York State attorney general.

The health-care subcommittee and its parent panel, the House Commerce Committee, are holding hearings on various aspects of the proposed tobacco settlement as a prelude to the expected enactment of comprehensive legislation next year. Senate hearings have already concluded, and both houses are expected to begin drafting legislation in January.

THE WALL STREET JOURNAL
WEDNESDAY, DECEMBER 10, 1997

MEMORANDUM

TO: ELENA KAGAN
CC: JERRY MANDE
FROM: TOM FREEDMAN, MARY L. SMITH
RE: TOBACCO SMUGGLING: ATF EFFORTS
DATE: AUGUST 26, 1997

SUMMARY

In speaking with ATF, ATF reports that it does not have a coordinated, nationwide effort to combat tobacco smuggling. ATF does become involved in tobacco smuggling on a case-by-case basis. However, given that ATF's budget has remained relatively steady in the past few years, ATF focuses its resources on more violent crimes. In addition, ATF has allocated more of its resources to dealing with other Administration priorities such as church fires, militias, and youth gun crimes. With respect to the tobacco smuggling cases in which ATF has been involved, these cases have tended to be the more egregious cases.

ATF also deals with tobacco smuggling within the 50 states. For instance, because Virginia has one of the lowest tax rates on cigarettes, many persons buy cigarettes in Virginia and smuggle them out of state.

ATF reports that the cases that have involved tobacco company employees are the ones in Syracuse and New Orleans, as reported in the N.Y. Times on August 25, 1997. As an aside, ATF notes that generally RJ Reynolds has been more concerned with preventing smuggling than has Philip Morris.

- \$45 million with cards bearing Visa and MasterCard logos.
- 40% if U.S. financial institutions had debit cards, up from 32% from 1994. Consumers who used their check cards 10 times per month doubled from 1994 to 1996. (American Banker Survey, December 1996).

BACKGROUND

Debit cards, also called check cards, are a cross between an ATM card and a credit card. They are issued by banks in conjunction with a major credit card, such as Visa or MasterCard, and can be used at any store that accepts credit cards.

When using a debit card at an ATM, the cardholder is required to punch in a Personal Identification Number, or PIN, as a precaution against fraud. When using a debit card with a merchant, however, only a signature and not a PIN is required.

Under current law, check cards are regulated by the Electronic Funds Transfer Act, the law which oversees ATM cards. This law provides for a maximum liability to consumers of \$50 if the card is reported lost or stolen within 24 hours, \$500 if reported within 60 days, and unlimited liability thereafter. The Truth in Lending Act, which regulates credit cards, has a maximum liability of \$50.

**Subtitle ____—Prevention of
Tobacco Smuggling**

SEC. ____01. DEFINITIONS.

In this subtitle:

(1) **AFFILIATE.**—The term “affiliate” means any one of 2 or more persons if 1 of such persons has actual or legal control, directly or indirectly, whether by stock ownership or otherwise, of the other or others of such persons, and any one of 2 or more persons subject to common control, actual or legal, directly or indirectly, whether by stock ownership or otherwise.

(2) **CIGAR.**—The term “cigar” means any roll of tobacco wrapped in leaf tobacco or in any substance containing tobacco (other than any roll of tobacco which is a cigarette or cigarillo within the meaning of paragraph (3) or (4)).

(3) **CIGARETTE.**—The term “cigarette” means any product which contains nicotine, is intended to be burned under ordinary conditions of use, and consists of—

(A) any roll of tobacco wrapped in paper or in any substance not containing tobacco; and

(B) any roll of tobacco wrapped in any substance containing tobacco which, because of

1 its appearance, the type of tobacco used in the
2 filler, or its packaging and labeling, is likely to
3 be offered to, or purchased by, consumers as a
4 cigarette described in subparagraph (A).

5 (4) CIGARILLOS.—The term “cigarillos” means
6 any roll of tobacco wrapped in leaf tobacco or any
7 substance containing tobacco (other than any roll of
8 tobacco which is a cigarette within the meaning of
9 paragraph (3)) and as to which 1,000 units weigh
10 not more than 3 pounds.

11 (5) CIGARETTE TOBACCO.—The term “cigarette
12 tobacco” means any product that consists of loose
13 tobacco that contains or delivers nicotine and is in-
14 tended for use by persons in a cigarette. Unless oth-
15 erwise stated, the requirements of this Act pertain-
16 ing to cigarettes shall also apply to cigarette to-
17 bacco.

18 (6) INTERSTATE OR FOREIGN COMMERCE.—The
19 term “interstate or foreign commerce” means com-
20 merce between any State and any place outside
21 thereof, or commerce within any Territory or the
22 District of Columbia, or between points within the
23 same State but through any place outside thereof.

24 (7) LITTLE CIGAR.—The term “little cigar”
25 means any roll of tobacco wrapped in leaf tobacco or

1 any substance containing tobacco (other than any
2 roll of tobacco which is a cigarette within the mean-
3 ing of subsection (1)) and as to which 1,000 units
4 weigh not more than 3 pounds.

5 (8) PERSON.—The term “person” means indi-
6 vidual, partnership, joint stock company, business
7 trust, association, corporation, or other form of busi-
8 ness enterprise, including a receiver, trustee, or liq-
9 uidating agent and including an officer or employee
10 of any agency of a State or political subdivision
11 thereof.

12 (9) PIPE TOBACCO.—The term “pipe tobacco”
13 means any loose tobacco that, because of its appear-
14 ance, type, packaging, or labeling, is likely to be of-
15 fered to, or purchased by, consumers as a tobacco
16 product to be smoked in a pipe.

17 (10) ROLL-YOUR-OWN TOBACCO.—The term
18 “roll-your-own tobacco” means any tobacco which,
19 because of its appearance, type, packaging, or label-
20 ing, is suitable for use and likely to be offered to,
21 or purchased by, consumers as tobacco for making
22 cigarettes.

23 (11) SECRETARY.—The term “Secretary”
24 means the Secretary of the Treasury.

1 (12) SMOKELESS TOBACCO.—The term “smoke-
2 less tobacco” means any product that consists of
3 cut, ground, powdered, or leaf tobacco that contains
4 nicotine and that is intended to be placed in the oral
5 or nasal cavity.

6 (13) TOBACCO PRODUCT.—The term “tobacco
7 product” means cigarettes, cigarillos, cigarette to-
8 bacco, little cigars, pipe tobacco, smokeless tobacco,
9 and roll-your-own tobacco.

10 (14) UNITED STATES.—The term “United
11 States” means the several States and Territories
12 and the District of Columbia. The term “State” in-
13 cludes a Territory and the District of Columbia. The
14 term “Territory” means Alaska, Hawaii, and Puerto
15 Rico.

16 SEC. ____02. PROHIBITIONS.

17 (a) IMPORTATION AND SALE.—It shall be unlawful,
18 except pursuant to a permit issued by the Secretary under
19 section ____08—

20 (1) to engage in the business of importing into
21 the United States tobacco products; or

22 (2) for any person so engaged to sell, offer, or
23 deliver for sale, contract to sell, or ship, in interstate
24 or foreign commerce, directly or indirectly or
25 through affiliate, tobacco products so imported.

1 (b) MANUFACTURE AND SALE.—It shall be unlawful,
2 except pursuant to a permit issued by the Secretary under
3 section ____03—

4 (1) to engage in the business of manufacturing,
5 packaging or warehousing tobacco products; or

6 (2) for any person so engaged to sell, offer, or
7 deliver for sale, contract to sell, or ship, in interstate
8 or foreign commerce, directly or indirectly or
9 through an affiliate, tobacco products so manufac-
10 tured, packaged or warehoused.

11 (c) WHOLESALE.—It shall be unlawful, except pursu-
12 ant to a permit issued by the Secretary under section
13 ____03—

14 (1) to engage in the business of purchasing for
15 resale at wholesale tobacco products; or

16 (2) for any person so engaged to receive or sell,
17 offer or deliver for sale, contract to sell, or ship, in
18 interstate or foreign commerce, directly or indirectly
19 or through an affiliate, tobacco products so pur-
20 chased.

21 (d) NONAPPLICATION.—This section shall not apply
22 to any agency of a State or political subdivision thereof
23 or any officer or employee of any such agency, and no
24 such agency or officer or employee shall be required to
25 obtain a permit under this subtitle.

1 (e) **EFFECTIVE DATE.**—The provisions of this section
2 shall become effective on the date that is 180 days after
3 the date of enactment of this subtitle.

4 **SEC. ____ OS. TOBACCO PRODUCT PERMITS.**

5 (a) **ENTITLEMENT.**—A person shall be entitled to re-
6 ceive a tobacco product permit if—

7 (1) such person submits an application for such
8 permit to the Secretary;

9 (2) the Secretary determines that such person
10 (or in case of a corporation, any of its officers, direc-
11 tors, or principal stockholders) has not—

12 (A) been convicted of a felony under Fed-
13 eral or State law; or

14 (B) during the 3-year period prior to date
15 of the submission of such application, been con-
16 victed of a misdemeanor under any Federal law
17 relating to a tobacco product, including the tax-
18 ation thereof;

19 (3) the Secretary determines that such person
20 is, by reason of the business experience, financial
21 standing, or trade connections of the person, likely
22 to—

23 (A) commence operations under the permit
24 within a reasonable period of time; or

1 (B) maintain such operations in conformity
2 with Federal law; and

3 (4) the Secretary determines that the tobacco
4 product operations proposed to be conducted by such
5 person under the permit are not in violation of the
6 law of the State in which they are to be conducted.

7 (b) APPLICATION.—

8 (1) IN GENERAL.—The Secretary shall pre-
9 scribe the manner and form of applications for to-
10 bacco product permits (including the facts to be set
11 forth therein) and the form of all such permits, and
12 shall specify in any such permit the authority that
13 is conferred by the permit and the conditions thereof
14 in accordance with the provisions of this subtitle.

15 (2) SEPARATE APPLICATION OR PERMIT.—To
16 the extent determined necessary by the Secretary for
17 the efficient administration of this subtitle, separate
18 applications and permits may be required by the
19 Secretary with respect to different types of tobacco
20 products, and with respect to the various classes of
21 persons entitled to permits under subsection (a).

22 (c) CONDITIONS.—A tobacco product permit shall be
23 conditioned upon the compliance of the person with the
24 requirements of this subtitle and with all other Federal

1 laws relating to tobacco products, including taxes with re-
2 spect thereto.

3 (d) REFUSAL OF PERMIT; HEARING.—

4 (1) IN GENERAL.—If upon the examination of
5 any application for a tobacco product permit under
6 subsection (a) the Secretary has reason to believe
7 that the applicant does not meet the requirements of
8 such subsection, the Secretary shall notify the appli-
9 cant thereof and, upon request by the applicant, af-
10 ford such applicant due notice and an opportunity
11 for a hearing on the application.

12 (2) DETERMINATION.—If the Secretary, after
13 notice and an opportunity for a hearing under para-
14 graph (1), determines that the applicant does not
15 meet the requirements of subsection (a), the Sec-
16 retary shall by order deny the application and state
17 the findings which are the basis for such order.

18 (e) REVOCATION, SUSPENSION AND ANNULMENT.—

19 (1) IN GENERAL.—A tobacco product permit
20 shall by order of the Secretary, after due notice and
21 an opportunity for a hearing to the permit holder—

22 (A) be revoked, or suspended for such pe-
23 riod as the Secretary determines appropriate, if
24 the Secretary finds that the permit holder has
25 willfully violated any of the conditions of the

1 permit, except that with respect to a first viola-
2 tion of the conditions of the permit, the Sec-
3 retary may only suspend such permit;

4 (B) be revoked if the Secretary finds that
5 the permit holder has not engaged in the oper-
6 ations authorized by the permit for a period of
7 more than 2 years; or

8 (C) be annulled if the Secretary finds that
9 the permit was procured through fraud, or mis-
10 representation, or concealment of a material
11 fact.

12 (2) FINDINGS.—An order under paragraph (1)
13 shall state the findings which are the basis for the
14 order.

15 (f) DURATION OF PERMIT.—

16 (1) IN GENERAL.—A tobacco product permit
17 shall continue in effect until suspended, revoked, or
18 annulled as provided for in subsection (e), or volun-
19 tarily surrendered by the permit holder, except that
20 if such permit is transferred by operation of law or
21 if actual or legal control of the permit holder is ac-
22 quired, directly or indirectly, whether by stock-own-
23 ership or in any other manner, by any person, then
24 such permit shall be automatically terminated upon
25 the expiration of the 30-day period beginning on the

1 date of such transfer or acquisition. If within such
2 30-day period an application for a new tobacco prod-
3 uct permit is made by the transferee or acquiring
4 person, respectively, then the outstanding permit
5 shall continue in effect until such application is fi-
6 nally acted on by the Secretary.

7 (2) LIMITATION.—Except as provided in para-
8 graph (1), a permit under this section may not be
9 transferred.

10 (g) SERVICE OF ORDERS.—Orders of the Secretary
11 with respect to the denial of a permit, the suspension, rev-
12 ocation or annulment of a permit, or any other proceeding,
13 shall be served—

14 (1) in person by any officer or employee of the
15 Secretary or any internal revenue or customs officer
16 authorized by the Secretary for that purpose; or

17 (2) by mailing the order by registered mail, ad-
18 dressed to the applicant or permit holder at the last
19 known address as contained in the records of the
20 Secretary.

21 (h) APPEAL; PROCEDURE.—

22 (1) IN GENERAL.—An appeal may be taken by
23 a permit holder or applicant for a permit from any
24 order of the Secretary denying such application, or
25 suspending, revoking, or annulling, a permit. Such

1 appeal shall be taken by filing, within 60 days after
2 the date on which such order is entered, a written
3 petition praying that the order of the Secretary be
4 modified or set aside in whole or in part, in the
5 court of appeals of the United States within any cir-
6 cuit wherein such permit holder or applicant resides
7 or has its principal place of business, or in the Unit-
8 ed States Court of Appeals for the District of Co-
9 lumbia.

10 (2) RECORDS.— A copy of the petition under
11 paragraph (1) shall be forthwith transmitted by the
12 clerk of the court to the Secretary, or any officer
13 designated by Secretary for that purpose, and there-
14 upon the Secretary shall file in the court the record
15 upon which the order complained of was entered, as
16 provided for under section 2112 of title 28.

17 (3) JURISDICTION.—Upon the filing of a peti-
18 tion under paragraph (1), the court shall have exclu-
19 sive jurisdiction to affirm, modify, or set aside the
20 order involved, in whole or in part.

21 (4) GROUNDS FOR OBJECTION.—No objection
22 to an order of the Secretary shall be considered by
23 the court under this subsection unless such objection
24 shall have been urged before the Secretary or unless
25 there were reasonable grounds for failure to do so.

1 (5) FINDINGS OF FACT.—The finding of the
2 Secretary as to the facts in any action under this
3 subsection, if supported by substantial evidence,
4 shall be conclusive. If any party shall apply to the
5 court for leave to adduce additional evidence, and
6 shall demonstrate to the satisfaction of the court
7 that such additional evidence is material and that
8 there were reasonable grounds for failure to adduce
9 such evidence in the proceeding before the Secretary,
10 the court may order such additional evidence to be
11 taken before the Secretary and to be adduced upon
12 the hearing in such manner and upon such terms
13 and conditions as to the court may seem proper. The
14 Secretary may modify his findings as to the facts by
15 reason of the additional evidence so taken, and shall
16 file with the court such modified or new findings,
17 which, if supported by substantial evidence, shall be
18 conclusive, and the recommendation, if any, of the
19 Secretary for the modification or setting aside of the
20 original order.

21 (6) JUDGMENT OF COURT.—The judgment and
22 decree of the court under this subsection affirming,
23 modifying, or setting aside, in whole or in part, any
24 order of the Secretary under this section shall be
25 final, subject to review by the Supreme Court of the

1 United States upon certiorari or certification as pro-
2 vided for in sections 346 and 347 of title 28.

3 (7) STAY OF ORDER.—The commencement of
4 proceedings under this subsection shall, unless spe-
5 cifically ordered by the court to the contrary, oper-
6 ate as a stay of the Secretary's order.

7 (i) LIMITATION.—No proceeding for the suspension
8 or revocation of a tobacco product permit for a violation
9 of any condition thereof relating to compliance with Fed-
10 eral law shall be instituted by the Secretary more than
11 18 months after the date on which a conviction of the vio-
12 lation of Federal law, or, if no conviction has been had,
13 more than 3 years after the date on which the violation,
14 and no such permit shall be suspended or revoked for a
15 violation of any such condition if the alleged violation of
16 Federal law has been compromised by any officer of the
17 Federal Government authorized to compromise such viola-
18 tion.

19 (j) NO DEPRIVATION OF REMEDY.—The issuance of
20 a tobacco product permit under this section shall not oper-
21 ate to deprive the United States of its remedy for any vio-
22 lation of law.

1 SEC. ____04. TOBACCO PRODUCT LABELING REQUIRE-
2 MENTS.

3 (a) IN GENERAL.—It shall be unlawful for any per-
4 son to sell or ship or deliver for sale or shipment, or other-
5 wise introduce in interstate or foreign commerce, or to re-
6 ceive therein, or to remove from customs custody for use,
7 any tobacco product unless such product is packaged and
8 labeled in conformity with this section.

9 (b) CERTIFICATE.—

10 (1) IN GENERAL.—It shall be unlawful for any
11 person to sell, offer, or deliver for sale, contract to
12 sell, or ship, in interstate or foreign commerce, di-
13 rectly or indirectly or through an affiliate, tobacco
14 products, except pursuant to a certificate issued by
15 the Secretary under paragraph (2).

16 (2) REQUIREMENTS.—A person shall be enti-
17 tled to receive a tobacco product certificate if—

18 (A) such person submits an application for
19 such a certificate to the Secretary;

20 (B) such person has in effect a permit
21 under section ____03 that applies to the to-
22 bacco products for which such person seeks a
23 certificate under this subsection; and

24 (C) the Secretary determines, based on the
25 application, that the tobacco products involved
26 are labeled in accordance with this section.

1 (c) LABELING.—

2 (1) CHAIN OF CUSTODY STAMPS.—Not later
3 than 1 year after the date of enactment of this sub-
4 title, the Secretary shall promulgate regulations that
5 require a chain of custody stamp to appear on the
6 package of each tobacco product manufactured or
7 distributed in the United States.

8 (2) REQUIREMENTS.—The regulations under
9 paragraph (1) shall require that each chain of cus-
10 tody stamp—

11 (A) utilize secure bar code technology that
12 permits foreign and domestic governmental offi-
13 cials to obtain information as to the chain of
14 custody of the tobacco product;

15 (B) contain information that identifies—

16 (i) the facility at which such tobacco
17 product was manufactured, including the
18 city and State in which such facility is lo-
19 cated;

20 (ii) the facility which distributed the
21 tobacco product (if any);

22 (iii) the export facility or warehouse
23 in which the tobacco product was stored (if
24 any); and

1 (iv) the country of final destination of
2 the tobacco product;

3 (C) be of a certain size and appear at a
4 specific location on each package of a tobacco
5 product; and

6 (D) contain any other information deter-
7 mines appropriate by the Secretary to establish
8 the chain of custody of the tobacco product.

9 (d) ENFORCEMENT.—

10 (1) REVOCATION OF PERMIT.—If the Secretary
11 determines that a person is not in compliance with
12 the requirements of this section, or is manufacturing
13 or distributing tobacco products without a certifi-
14 cate, the Secretary shall revoke the tobacco product
15 permit of the person under section ____03.

16 (2) REMOVAL.—In order to prevent the sale or
17 shipment or other introduction of tobacco products
18 in interstate or foreign commerce in violation of the
19 requirements of this section, no person shall remove
20 from customs custody, for sale or any other commer-
21 cial purpose, tobacco products unless such person
22 has obtained a certificate under this section covering
23 such products

24 (3) RELEASE.—In order to prevent the sale or
25 shipment or other introduction of tobacco products

1 in interstate or foreign commerce in violation of the
2 requirements of this section, Officers of the Internal
3 Revenue Service are authorized and directed to with-
4 hold the release of tobacco products from the manu-
5 facturer or distributor unless a certificate covering
6 such products has been obtained.

7 (4) JURISDICTION OF COURTS.—The District
8 Courts of the United States, and the United States
9 court for any Territory, shall have jurisdiction of
10 suits to enjoin, annul, or suspend in whole or in part
11 any final action by any Federal official under this
12 subsection.

13 (e) PROHIBITION ON ALTERATION.—It shall be un-
14 lawful for any person to alter, mutilate, destroy, obliterate,
15 or remove any stamp or label upon a tobacco product held
16 for sale in interstate or foreign commerce or after ship-
17 ment therein, except as authorized by Federal law or ex-
18 cept pursuant to regulations of the Secretary authorizing
19 relabeling for purposes of compliance with the require-
20 ments of this section or of State law.

21 SEC. ____05. REQUIREMENTS FOR THE TRACKING OF TO-
22 BACCO PRODUCTS.

23 (a) POSTING OF BOND.—

1 (1) IN GENERAL.—It shall be unlawful for any
2 person to export any tobacco product unless such
3 person—

4 (A) has posted with the Secretary a to-
5 bacco product bond in accordance with this sec-
6 tion for such product that contains a disclosure
7 of the country to which such product will be ex-
8 ported; and

9 (B) determines that the recipient of such
10 products in such country will not violate any
11 law or regulation of such country with respect
12 to such products.

13 (2) REGULATIONS.—The Secretary shall pro-
14 mulgate regulations that determine the amount of
15 each bond that must be posted under paragraph (1).

16 (b) RETURN OF BOND.—The Secretary shall return
17 a bond posted under subsection (a) upon a determination
18 by the Secretary (based on documentation provided by the
19 person who posted the bond in accordance with regulations
20 promulgated by the Secretary) that—

21 (1) the tobacco products to which the bond ap-
22 plies have been received in the country of final des-
23 tination as designated in the bond; and

1 (2) such country of final destination is a coun-
2 try which appears on the approved country list
3 under subsection (c).

4 (c) APPROVED COUNTRY LIST.—

5 (1) DETERMINATION.—The Secretary shall an-
6 nually determine which countries—

7 (A) present a legitimate foreign market for
8 tobacco products exported from the United
9 States; and

10 (B) refrain from transshipping tobacco
11 products exported from the United States to
12 other countries.

13 (2) LIST.—The Secretary shall annually com-
14 pile an public in the Federal Register a list of coun-
15 tries determined to be in compliance with subpara-
16 graphs (A) and (B) of paragraph (1).

17 **SEC. ____08. PRICING OF PRODUCTS SOLD ON MILITARY IN-**
18 **STALLATIONS OR BY NATIVE AMERICANS.**

19 (a) MILITARY INSTALLATIONS.—The Secretary, in
20 consultation with the Secretary of Defense, shall promul-
21 gate regulations that ensure that the price charged for a
22 tobacco product sold on a military installation (as defined
23 in section 2801(c)(2) of title X, United States Code) is
24 equal to—

1 (1) the highest price for which such product is
2 sold in the country in which the military installation
3 is located; or

4 (2) the highest price (inclusive of Federal or
5 State taxes) for which such product is sold in the
6 United States;
7 whichever is greater.

8 (b) INDIAN TRIBES.—The Secretary, in consultation
9 with the Secretary of Interior, shall promulgate regula-
10 tions that ensure that the price charged for a tobacco
11 product sold on an Indian reservation (as defined in sec-
12 tion 403(9) of the Indian Child Protection and Family Vi-
13 olence Prevention Act (25 U.S.C. 3202(9))), or by an In-
14 dian tribe or tribal organization (as such terms are defined
15 in section 4 of the Indian Self Determination and Edu-
16 cation Assistance Act (25 U.S.C. 450b)), is equal to the
17 highest price (inclusive of Federal or State taxes) for
18 which such product is otherwise sold in the United States.

19 SEC. ____07. **PROHIBITION AGAINST SALE OF TOBACCO**
20 **PRODUCTS IN DUTY-FREE SHOPS.**

21 It shall be unlawful for any person to sell a tobacco
22 product in any duty-free shop located within the United
23 States.

1 SEC. ____ 98. JURISDICTION; PENALTIES; COMPROMISE OF
2 LIABILITY.

3 (a) JURISDICTION.—The District Courts of the Unit-
4 ed States, and the United States court for any Territory,
5 of the District where the offense is committed or threat-
6 ened or of which the offender is an inhabitant or has its
7 principal place of business, are vested with jurisdiction of
8 any suit brought by the Attorney General in the name of
9 the United States, to prevent and restrain violations of
10 any of the provisions of this subtitle.

11 (b) PENALTIES.—Any person violating any of the
12 provisions of this subtitle shall be guilty of a misdemeanor
13 and upon conviction thereof be fined not more than \$1,000
14 for each offense.

15 (c) COMPROMISE OF LIABILITY.—The Secretary is
16 authorized, with respect to any violation of this subtitle,
17 to compromise the liability arising with respect to a viola-
18 tion of this subtitle—

19 (1) upon payment of a sum not in excess of
20 \$500 for each offense, to be collected by the Sec-
21 retary and to be paid into the Treasury as mis-
22 cellaneous receipts; and

23 (2) in the case of repetitious violations and in
24 order to avoid multiplicity of criminal proceedings,
25 upon agreement to a stipulation, that the United
26 States may, on its own motion upon 5 days' notice

- 1 to the violator, cause a consent decree to be entered
- 2 by any court of competent jurisdiction enjoining the
- 3 repetition of such violation.

Tom

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*Smuggling
John W. Magaw*

LW
Opening Statement
John W. Magaw
Director
Bureau of Alcohol, Tobacco and Firearms
before the
House Commerce Committee

December 9, 1997

12-18-97.

*Bruce,
For your
records, some
documents
re: tobacco
smuggling, etc.
May
Tom*

Thank you, Mr. Chairman, members of the Committee. I appreciate this opportunity to better acquaint you with ATF's mission, and specifically, its role in preventing and investigating tobacco diversion.

History

For those of you not familiar with the Bureau's functions, let me tell you briefly a little about ATF's mission. In 1791, the nation's first tax was imposed on distilled spirits. This tax led to an uprising known as the Whiskey Rebellion, to which Treasury Secretary Alexander Hamilton dispatched the militia to put down the uprising. Over the years, ATF, and its predecessor, the Alcohol and Tax Unit of the Internal Revenue Service (IRS), has been charged by Congress with the regulation, taxation and criminal enforcement jurisdiction over violations of firearms, explosives, alcohol and tobacco laws.

The common thread in ATF's responsibilities over these varied products is they all are both legal commodities produced by a highly regulated industry and are also controversial products that have been traditionally susceptible to criminal diversion and misuse or abuse.

Mission

ATF's mission is three-fold: to reduce violent crime; to collect revenue; and to protect the public. We accomplish this with an integrated approach using regulatory inspectors, auditors, chemists, criminal investigators, and other specialists. And might I add, we are very good at what we do. For the past two years, ATF has been awarded the highest rating possible on its annual CFO audits by the Treasury Inspector General. We have learned from years of experience that, in many cases, voluntary compliance by the regulated industry can be achieved and criminal misuse and diversion can be prevented by regulatory oversight. The area of tobacco diversion is a prime example of the interactive nature of ATF's resources and authority. Ensuring that the industry is complying with regulatory and tax requirements can help prevent criminal diversion.

Jurisdiction

In 1978, Congress passed the Contraband Cigarette Trafficking Act, giving ATF the authority to investigate interstate diversion of cigarettes in avoidance of paying state tax, by prohibiting the shipment, transportation, or possession of more than 60,000 cigarettes (which equates to 3,000 packs or 300 cartons) not bearing indicia (or tax stamp) of evidence of tax payment in States that require such evidence. With this and other statutes, ATF's mandate to assist state and local governments has become a significant part of its mission. Originally enacted to prevent sales on the street, the problem of cigarette smuggling has become large commercial operations resulting

in these cigarettes ending up on retail shelves and distribution by organized crime.

Other statutes which can be applied in these cases include the Internal Revenue Code (IRC) and the Racketeer Influenced and Corrupt Organizations Act (RICO). ATF's goal is to achieve compliance with U.S. laws and to close the avenues to those involved in illegal diversion.

Extent of the Problem

In recent years, some foreign governments and certain state government have imposed a higher excise tax on tobacco products, thus creating a lucrative black market. Diversion involves products for both export and domestic consumption from a manufacturer to individuals acting as a broker or wholesaler. Rather than shipping the product to the destination stated on required Federal records, the product is diverted and sold illegally. Traceability is lost as goods disappear from legal commerce. Some wholesalers have been found to be the sources of supply, with retailers becoming increasingly active in these illegal sales. Unlike tobacco manufacturers, tobacco wholesalers and retailers are not statutorily required to hold permits and licenses issued by ATF.

For example, due to extremely high Canadian taxes on tobacco, significant quantities of U.S. manufactured tobacco products are smuggled into Canada. In addition, large amounts of Canadian manufactured tobacco products are "exported" into the United States and then smuggled back into Canada. As a result of this smuggling, Canada has lost billions of dollars in

tax revenues.

In addition, there has been a significant increase in trafficking in cigarettes from States with low taxes on tobacco to States with high taxes on tobacco. In a survey ATF conducted earlier this year on behalf of the House Appropriations Committee, ATF received estimates from several states on revenue loss figures. The State of Michigan estimated losing approximately \$50 million a year to cigarette diversion. The State of Washington estimated losing around \$100 million per year from cigarettes diverted from low tax states. California estimates its annual loss to be approximately \$30 million a year. The full extent of loss nationwide is difficult to calculate as many states polled were unable to give an estimate of their annual losses.

To give you an idea of ATF's involvement in diversion cases, we currently have over 85 open alcohol or tobacco trafficking investigations. Although limited resources put limitations on the number and extent of the investigations ATF undertakes, our investigations have increased over 500 percent in the past five years. Since 1994, ATF has made assessments of over \$30.4 million from companies and individuals involved in tobacco and alcohol trafficking. Seizures of tobacco commodities in 1997 totaled \$1.1 million.

ATF's largest contraband cigarette trafficking investigation involved the trafficking of cigarettes from the state of Montana -- the Flathead Indian Reservation -- to Washington state. In this case, six persons were convicted of racketeering, and three persons pleaded guilty to Conspiracy to Commit Racketeering. The average jail time was three years, and the maximum was 12 to 15

years. Total penalties were \$4.7 million and this sum was split between the U.S. government, the states, and the tribes.

ATF has a current investigation open involving 21 persons indicted in New York as part of a joint ATF, RCMP, U.S. Customs, INS, IRS and New York State Enforcement investigation. This investigation involved a smuggling ring on the St. Regis Mohawk Indian Reservation. Those indicted include prominent Native Americans from the St. Regis/Akwesasne Reservation and individuals associated with a Buffalo organized crime family. The charges include money laundering and racketeering. The assets from illegal proceeds are in this case estimated at over \$500 million.

In addition to illegal trafficking by traditional organized crime groups and Native Americans, ATF has also uncovered involvement in cigarette smuggling by Russian, Middle Eastern, and Asian organized crime groups. Investigation has revealed that these groups are also involved in firearms and narcotics trafficking, alien smuggling, and other illegal activities.

Over the past several years, alcohol and tobacco crimes have grown larger and more complex and have extended to both interstate and international investigations. Diversion cases often include nationwide activities since the smuggled goods are acquired in one part of the country and may be distributed unlawfully in another far away part of the country. In recognition of this national scope, ATF has established a Diversion Branch in Bureau Headquarters to coordinate and monitor these investigations. An Alcohol and Tobacco Database has also been developed to

track diversion and trafficking activity.

Due to a substantial loss of revenue and a heightened awareness, many states have requested ATF's assistance in helping to eliminate this problem. Through our efforts to eradicate this problem, ATF, in cooperation with the Federation of Tax Administrators, has established a 24-hour cigarette hotline, 1-800-659-6242, to report stolen, hijacked or seized cigarettes. You can be assured of our commitment to assisting state and local governments in their efforts to combat cigarette diversion.

On the international level, ATF maintains ongoing liaison with foreign law and revenue enforcement authorities, such as the Royal Canadian Mounted Police (RCMP) and Revenue Canada, to ascertain the scope of cigarette trafficking worldwide. The Bureau also is working closely with criminal investigators and tax officials in East European countries to develop and implement criminal and regulatory enforcement schemes with respect to cigarettes.

Finally, ATF has worked, through the issuance of Industry Circulars and meetings, to ensure that legitimate members of the tobacco industry do not facilitate illicit tobacco trafficking.

Thank you, again, for the opportunity to appear before your committee today. I would be happy to answer any questions you may have.

Draft language regarding tobacco product labeling and advertising abroad

SEC. 1. EXPORTS OF TOBACCO PRODUCTS ABROAD

(1) **REQUIREMENTS** --It shall be unlawful for any domestic concern to export from the United States, or to sell or distribute in, or export from, any other country, any tobacco products the package of which does not contain a warning label that--

(A) complies with Federal labeling requirements for cigarettes manufactured, imported, or packaged for sale or distribution within the United States; and

(B) is in the primary language of the country in which the cigarettes are intended for consumption.

(2) **WAIVERS** --The President may waive the prohibition contained in paragraph (1) if the President determines that the country in which the exported tobacco products are intended for consumption has in effect requirements for labeling of tobacco product packages substantially similar to or more stringent than the requirements for labeling of tobacco products set forth in paragraph (1).

SEC. 2. ADVERTISING OF TOBACCO PRODUCTS ABROAD

(1) **REQUIREMENTS** --It shall be unlawful for any domestic concern to advertise or cause to be advertised abroad any tobacco product in a manner that does not comply with Federal requirements for the advertisement of tobacco products in the United States.

SEC. 3. PENALTIES.

(1) **FINE** --Any person who violates the provisions of section 1 or section 2 shall be fined not more than \$100,000 per day for each such violation. Any person who knowingly reexports from or transships tobacco products through a foreign country for which the President has issued a waiver as described in section 1(2) to avoid the requirements of section 1 shall be fined not more than \$150,000 per day for each such occurrence.

(2) **INJUNCTION PROCEEDINGS** --The district courts of the United States shall have jurisdiction, for cause shown, to prevent and restrain violations of section 1 or section 2 upon the application of the Attorney General of the United States.

SEC. 4. DEFINITIONS.

(1) **DOMESTIC CONCERN** --In this act, the term "domestic concern" means--

(A) any individual who is a citizen, national, or resident of the United States; and

(B) any corporation, partnership, association, joint-stock company, business trust, unincorporated organization, or sole proprietorship which has its principal place of business in the United States, or which is organized under the laws of a State of the United States or a territory, possession, or commonwealth of the United States.

*Subsidiary
concern*

ECTA

Memorandum

To: Int'l tobacco working group
From: Cathy Carpino
Date: December 18, 1997
Subject: Outline of anti-smuggling proposal

I. Establish a permit system for cigarettes: Mirroring the system in place for alcohol (27 USC 203, et seq), this proposal would require any person engaged in the business of manufacturing, distributing, selling, or importing tobacco to obtain a permit from the Treasury Secretary within a certain period of time (e.g., 180 days) of enactment of Act. Any person shall be entitled to a permit unless they have been convicted of a felony, convicted of a misdemeanor involving tobacco within the past three years, or if such person is unlikely to conform their operations with federal law.

The Secretary may suspend, revoke, or annul a permit if any of the permit's conditions are violated. These permits cannot be transferred voluntarily. If transferred by operation of law, the new permittee shall have 30 days within which to reapply. The old permit shall continue in effect until the Secretary acts on the permittee's application.

To prevent the sale or distribution of cigarette packages that do not comply with federal labeling requirements, no person shall produce, distribute, or sell cigarettes unless that person obtains a certificate from the Secretary. Officers of internal revenue are authorized and directed to withhold the release of packages of cigarettes from the manufacturer unless such a certificate has been obtained. Customs officers are authorized and directed to withhold the release of packages of cigarettes from customs custody unless certificates have been obtained. [need to look at the Kennedy bill and Conrad's proposal to ensure consistency]

II. New labeling requirements for cigarette packages: (1) The President is directed to require cigarette manufacturers to identify the manufacturing facility, distribution facility, export warehouse, and any other information determined by the President to be relevant to the chain of custody on each package of cigarettes within one year of enactment of this Act. The stamp containing this information shall use secure technology that is not susceptible to

alteration, but that can be accessed by officials, both in the United States and in foreign countries, and (2) Cigarette manufacturers shall label every package with the country of final destination. The President shall promulgate regulations regarding the size and location of this stamp on the package. If manufacturers do not comply with federal labeling requirements, the Secretary of Treasury shall revoke their permit, in addition to applying all existing penalties.

III. Tracking requirements: (1) Cigarette manufacturers are required to post a bond for exported packages of cigarettes to be returned when the Secretary of Treasury receives documentation that such cigarettes reached their final destination. The Secretary of Treasury shall promulgate regulations determining the amount of the bond and what documentation is needed to verify delivery of the packages; (2) in order to obtain the return of a bond, the Secretary shall determine that a country has a legitimate market for cigarettes exported from the United States and that such cigarettes are to be consumed in that country as part of the legitimate market. The Secretary shall publish the list of these countries; and (3) Cigarette manufacturers cannot sell to any person, either in the United States or in a foreign country, if they have reason to believe such person will violate any law or regulation of that country, or if such person was convicted of a crime involving cigarettes.

IV. Military bases: The Secretary of Defense is directed to require that packages of cigarettes sold overseas on military bases shall be priced at the highest level found in the country in which the base is located or in the United States, whichever is greater. Packages of cigarettes sold on military bases shall be so marked.

V. Indian reservations: Packages of cigarettes on Indian reservations shall be so marked.

VI. Duty-free stores: Duty-free stores located in the United States shall not sell packages of cigarettes and no person in the United States may sell to duty-free stores in foreign countries.

VII. Increased resources: It is the sense of the Senate that the Treasury Department shall allocate additional resources to curb the problem of cigarette smuggling, especially on Indian reservations.

AMERICAN CENTER FOR A TOBACCO-FREE WORLD

Sec. I FINDINGS

1) Tobacco use is estimated to have caused nearly 3 million deaths a year worldwide in the early 1990's, and is projected to cause in excess of 10 million additional deaths a year globally by 2025, making it the leading killer worldwide. More than 70% of those deaths are expected in developing countries.

2) Most developing governments are unprepared to address increases in tobacco deaths, including the impact on health systems and health costs. Very few have implemented the fiscal and regulatory policies that can limit increases in tobacco attributable deaths. While tobacco consumption in the U.S. and other established market economies has fallen over the last decade, consumption is rising in China, India, East Asia, and former socialist economies. Tobacco companies in the US and elsewhere have increasingly targeted these markets. ~~Along with China, Germany, and Japan, the US accounts for one-half of the global cigarette production.~~

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3) Tobacco use markedly reduces good health and threatens to erode the major health gains in life expectancy of the last century. Only HIV infection and tobacco are large and growing causes of death worldwide. The total projected deaths from tobacco over the next ten years likely will exceed deaths from HIV, maternal and childhood conditions and tuberculosis combined. ~~While the US has shown significant leadership in mobilizing international HIV control, it has done far less to prevent the spread of tobacco use.~~

4) ~~Since 1992, the World Bank has adopted a formal policy of not lending for tobacco production, processing, or marketing. The World Bank's conservative estimate is that tobacco investment globally resulted in an annual \$200 billion net economic loss around 1990. Any economic evaluation that places reasonable value on human life suggests a net loss from tobacco.~~

5) ~~The adoption of comprehensive national legislation governing tobacco will constitute necessary world leadership. No civilized society can do less to stem the toll of disease and death from tobacco use. Since marketing abuses that the US seeks to control at home are practiced without restraint abroad by US-based companies, there is both a public health and moral obligation to do the extent possible to see that the protections afforded US citizens are extended to all.~~

5) The United States consistently has provided leadership and funding to address the world's most pressing public health needs, including AIDS, hunger, maternal and child health, and immunization. (Annual U.S. funding for these public health issues exceeds \$XXX)

6) The United States exports more than 240 billion cigarettes per year worth more than \$6 billion. The leading American tobacco company made in excess of \$6.3 billion in overseas profits in 1996, ranking third in performance among transnational U.S.-based companies. Foreign sales now account for more than half of all sales for the two leading

U.S. tobacco manufacturers.

7) In light of the role the U.S. has played in spreading tobacco use globally, and in light of the large financial benefits the U.S. continues to enjoy from tobacco exports, it is appropriate that this nation provide significant assistance and funding for international public education and mass media programs that inform the public about the hazards of tobacco use.

8) Smoking in U.S. films is pervasive and influences persons in other countries who seek to emulate "American activities" depicted in motion pictures. A recent study recently reported that more than half of the top-grossing U.S. films released between 1991 and 1996 exhibited smoking. In these films, 80 percent of the male lead characters and 27 percent of the female characters smoked. The motion picture industry is painting a distorted picture that smoking is a truly American activity.

~~6) Remuneration for the death and disease caused by these profits is appropriate. At the very least, American policies governing advertising, production, labeling, packaging and sales at home must be consistent abroad.~~

SEC 2 PURPOSES. The American Center for a Tobacco-free World (ACT) shall assist organizations in other countries to address the several health problems associated with tobacco use through-

1) public education programs that inform the public about the hazards of tobacco use and of environmental tobacco smoke,

2) mass media campaigns, including paid counter-tobacco advertisements, to reverse the image appeal of pro-tobacco messages, especially those that glamorize and "Westernize" tobacco use to young people,

3) educating organizations about the economic and societal costs of tobacco use, and effective tobacco use prevention strategies that are appropriate for the country;

4) facilitating access to nicotine addiction therapies,

5) evaluating ^{and disseminating} tobacco use ^{or prevention} cessation strategies; and

6) providing technical assistance to develop standardized epidemiologic methodologies to monitor tobacco use

7) and other efforts to reduce tobacco use

SEC 3 DEFINITIONS.

(a) Trust fund _The term "Trust Fund" means the National Tobacco Settlement Trust Fund established in the Treasury of the United States consisting of amounts that are appropriated or accredited to the trust fund from the tobacco settlement approved by Congress

SEC 4. AMERICAN CENTER FOR A TOBACCO-FREE WORLD

Congress finds that there is established in the District of Columbia a private, nonprofit corporation known as American Center for a Tobacco-free World (ACT) which is neither an agency nor establishment of the United States Government

SEC 5 FUNDING

(a) ESTABLISHMENT OF GLOBAL PUBLIC HEALTH AND EDUCATION RESOURCE ACCOUNT . There is established with the Trust fund the Global Public Health and Education Resource Account that shall be accredited with \$ ___ for each fiscal year.

(b) IN GENERAL _The Secretary of the Treasury shall, on October 1 of each fiscal year subsequent to the effective date of this Act, transfer \$ ___ million from the Global Public Health and Education Resource Account of the Trust Fund to the account of the ACT to carry out the activities authorized under this Act

(c) TERMINATION OF TRANSFER AUTHORITY _The authority of the Secretary to transfer funds from the Trust Fund shall expire on ____

SEC. 6 ELIGIBILITY FOR ANNUAL TRANSFERS FROM THE TRUST FUND

(a) Nothing in this Act shall be construed to make the ACT an agency or establishment of the United States Government, or to make the members of the Board of the ACT, or its employees, officers or employees of the United States

(b) OVERSIGHT The ACT and its grantees shall be subject to the oversight and supervision of Congress, and shall annually submit a report of it's activities to ____

(c) CONDITIONS ON ELIGIBILITY FOR FUNDING (basically track language in sec 504 of PL 98-164- National Endowment for Democracy)

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meeting

SECTION 4. AMERICAN CENTER ON GLOBAL HEALTH AND TOBACCO

Congress finds that there is established in the District of Columbia a private, non-profit corporation known as the American Center (ACT) On Global Health and Tobacco which is neither an agency nor establishment of the United States Government.

ACT is governed by a Board of up to 25 members including:

1. On a bipartisan basis members of the Senate of the United States and of the House of Representatives.
2. The Presidents of American public health organizations.
3. The Presidents of American media, marketing and other non-government institutions and corporations.
4. Individuals active in education, public health, and other relevant activities.

ACT is to have an International Advisory Council. This Council consists of representatives from key global, regional and national public health organizations and leading individual educators and health professionals.

It is directed that ACT is to have a limited staff and to the maximum extent utilize the available experience and talents of existing American organizations to carry out its mandate. These include American non-governmental organizations with specialized international experience in health, education, media and tobacco.

SECTION 5. FUNDING

- (a) **ESTABLISHMENT OF GLOBAL PUBLIC HEALTH AND EDUCATION RESOURCE ACCOUNT.** There is established with the Trust Fund the Global Public Health and Education Resource Account that shall be accredited with \$150 million for each fiscal year.
- (b) **IN GENERAL.** The Secretary of the Treasury shall on October 1 of each fiscal year subsequent to the effective date of this Act, transfer \$150 million from the Global Public Health and Education Resource Account of the Trust Fund to the account of ACT to carry out the activities authorized under this Act.
- (c) **TERMINATION OF TRANSFER AUTHORITY.** The authority of the Secretary to transfer funds from the Trust Fund shall expire with the expiration of the Trust Fund.

SECTION 6. ELIGIBILITY FOR ANNUAL TRANSFERS FROM THE TRUST FUND.

- (a) Nothing in this Act shall be construed to make ACT an agency or establishment of the United States Government, or to make the members of the Board of ACT, or its employees, officers or employees of the United States.
- (b) **OVERSIGHT.** ACT and its grantees shall be subject to the oversight and supervision of Congress, and shall annually submit a report of its activities to the Congress.

(c) CONDITIONS FOR ELIGIBILITY FOR FUNDING.

a. Annual Payments from the Trust Fund may be made to ACT under this title only if ACT agrees to comply with the requirements specified in this section and elsewhere in this title.

b.1. ACT may only provide funding for programs of private sector groups and may not carry out programs directly.

2. ACT may provide funding only for programs which are consistent with the purposes set forth in Section 2.

Salary or
compensation

c.1. Officers of ACT may not receive any salary or other compensation from any source, other than ACT, for services rendered during the period of their employment by ACT.

Travel expenses.

2. If an individual who is an officer or employee of the United States Government serves as a member of the Board of Directors or as an officer or employee of ACT, that individual may not receive any compensation or travel expenses in connection with services performed for ACT.

Stock or
dividends.

d.1. ACT shall not issue any shares of stock or declare or pay any dividends.

2. No part of the assets of ACT shall inure to the benefit of any member of the Board, any officer or employee of ACT, or any other individual, except as salary or reasonable compensation for services.

Audits.

e.1. The accounts of ACT shall be audited annually in accordance with generally accepted auditing standards by independent certified public accountants or independent licensed public accountants certified or licensed by a regulatory authority of a State or other political subdivision of the United States. The audits shall be conducted at the place or places where the accounts of ACT are normally kept. All books, accounts, financial records, reports, files, and all other papers, things, or property belonging to or in use by ACT and necessary to facilitate the audits shall be made available to the person or persons conducting the audits; and full facilities for verifying transactions with any assets held by depositories, fiscal agents, and custodians shall be afforded to such person or persons.

Report.

2. The report of each such independent audit shall be included in the annual report required by subsection (h). The audit report shall set forth the scope of the audit and include such statements as are necessary to present fairly ACT's assets and liabilities, surplus or deficit, with an analysis of the changes therein during the year, supplemented in reasonable detail by a statement of ACT's income and expenses during the year, and a statement of the application of funds, together with the independent auditor's opinion of those statements.

GAO audit.

f.1. The financial transactions of ACT for each fiscal year may be audited by the General Accounting Office in accordance with such principles and procedures and under such rules and regulations as may be

prescribed by the Comptroller General of the United States. Any such audit shall be conducted at the place or places where accounts of ACT are normally kept. The representatives of the General Accounting Office shall have access to all books, accounts, records, reports, files, and all other papers, things, or property belonging to or in use by ACT pertaining to its financial transactions and necessary to facilitate the audit; and they shall be afforded full facilities for verifying transactions with any assets held by depositories, fiscal agents, and custodians. All such books, accounts, records, reports, files, papers, and property of ACT shall remain in the possession and custody of ACT.

Report to
Congress

2. A report of each such audit shall be made by the Comptroller General to the Congress. The report to the Congress shall contain such comments and information as the Comptroller General may deem necessary to inform the Congress of the financial operations and condition of ACT, together with such recommendations with respect thereto as he may deem advisable. The report shall also show specifically any program, expenditure, or other financial transaction or undertaking observed in the course of the audit which, in the opinion of the Comptroller General, has been carried on or made contrary to the requirements of this title. A copy of each report shall be furnished to the President and to ACT at the time submitted to the Congress.

Report to
President

Recordkeeping

g. 1. ACT shall ensure that each recipient of assistance provided through ACT under this title keeps such records as may be reasonably necessary to fully disclose the amount and the disposition by such recipient of the proceeds of such assistance, the total cost of the project or undertaking in connection with which such assistance is given or used, and the amount and nature of that portion of the cost of the project or undertaking supplied by other sources, and such other records as will facilitate an effective audit.

Information
accessibility

2. ACT shall ensure that it, or any of its duly authorized representatives, shall have access for the purpose of audit and examination to any books, documents, papers, and records of the recipient that are pertinent to assistance provided through ACT under this title. The Comptroller General of the United States or any of his duly authorized representatives shall also have access thereto for such purpose.

Report to
President and
Congress.

h. Not later than December 31 of each year, ACT shall submit an annual report for the preceding fiscal year to the President for transmittal to the Congress. The report shall include a comprehensive and detailed report of ACT's operations, activities, financial condition, and accomplishments under this title and may include such recommendations as ACT deems appropriate. The Board members and officers of ACT shall be available to testify before appropriate committees of the Congress with respect to such report, the report of any audit made by the Comptroller General pursuant to subsection (f), or any other matter which any such committee may determine.

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ant to this section shall be set forth in a grant agreement between the Secretary of State and The Asia Foundation.

(b) If funds made available to The Asia Foundation pursuant to this title or pursuant to any other provision of law are, with the permission of the head of the Federal agency making the funds available, invested by the Foundation or any of its subgrantees pending disbursement, the resulting interest is not required to be deposited in the United States Treasury if that interest is used for the purposes for which the funds were made available. Interest

FUNDING

SEC. 404. There are authorized to be appropriated to the Secretary of State \$5,000,000 for the fiscal year 1983, \$10,000,000 for the fiscal year 1984, and \$10,000,000 for the fiscal year 1985 for grants to The Asia Foundation pursuant to this title. 22 USC 4403.

TITLE V—NATIONAL ENDOWMENT FOR DEMOCRACY

National
Endowment for
Democracy Act.

SHORT TITLE

SEC. 501. This title may be cited as the "National Endowment for Democracy Act". 22 USC 4411
note.

NATIONAL ENDOWMENT FOR DEMOCRACY

SEC. 502. (a) The Congress finds that there has been established in the District of Columbia a private, nonprofit corporation known as the National Endowment for Democracy (hereafter in this title referred to as the "Endowment") which is not an agency or establishment of the United States Government. 22 USC 4411

(b) The purposes of the Endowment, as set forth in its articles of incorporation, are—

(1) to encourage free and democratic institutions throughout the world through private sector initiatives, including activities which promote the individual rights and freedoms (including internationally recognized human rights) which are essential to the functioning of democratic institutions;

(2) to facilitate exchanges between United States private sector groups (especially the two major American political parties, labor, and business) and democratic groups abroad;

(3) to promote United States nongovernmental participation (especially through the two major American political parties, labor, business, and other private sector groups) in democratic training programs and democratic institution-building abroad;

(4) to strengthen democratic electoral processes abroad through timely measures in cooperation with indigenous democratic forces;

(5) to support the participation of the two major American political parties, labor, business, and other United States private sector groups in fostering cooperation with those abroad dedicated to the cultural values, institutions, and organizations of democratic pluralism; and

(6) to encourage the establishment and growth of democratic development in a manner consistent both with the broad concerns of United States national interests and with the specific

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requirements of the democratic groups in other countries which are aided by programs funded by the Endowment.

GRANTS TO THE ENDOWMENT

22 USC 4412.

Sec. 503. (a) The Director of the United States Information Agency shall make an annual grant to the Endowment to enable the Endowment to carry out its purposes as specified in section 502(b). Such grants shall be made with funds specifically appropriated for grants to the Endowment or with funds appropriated to the Agency for the "Salaries and Expenses" account. Such grants shall be made pursuant to a grant agreement between the Director and the Endowment which requires that grant funds will only be used for activities which the Board of Directors of the Endowment determines are consistent with the purposes described in section 502(b), that the Endowment will allocate funds in accordance with subsection (a) of this section, and that the Endowment will otherwise comply with the requirements of this title. The grant agreement may not require the Endowment to comply with requirements other than those specified in this title.

(b) Funds so granted may be used by the Endowment to carry out the purposes described in section 502(a), and otherwise applicable limitations on the purposes for which funds appropriated to the United States Information Agency may be used shall not apply to funds granted to the Endowment.

Restriction.

(c) Nothing in this title shall be construed to make the Endowment an agency or establishment of the United States Government or to make the members of the Board of Directors of the Endowment, or the officers or employees of the Endowment, officers or employees of the United States.

(d) The Endowment and its grantees shall be subject to the appropriate oversight procedures of the Congress.

(e) Of the amounts made available to the Endowment for each of the fiscal years 1984 and 1985 to carry out programs in furtherance of the purposes of this Act—

(1) not less than \$13,800,000 shall be for the Free Trade Union Institute; and

(2) not less than \$2,800,000 shall be to support private enterprise development programs of the National Chamber Foundation.

ELIGIBILITY OF THE ENDOWMENT FOR GRANTS

22 USC 4413

Sec. 504. (a) Grants may be made to the Endowment under this title only if the Endowment agrees to comply with the requirements specified in this section and elsewhere in this title.

(b)(1) The Endowment may only provide funding for programs of private sector groups and may not carry out programs directly.

(2) The Endowment may provide funding only for programs which are consistent with the purposes set forth in section 502(b).

Salary or compensation.

(c)(1) Officers of the Endowment may not receive any salary or other compensation from any source, other than the Endowment, for services rendered during the period of their employment by the Endowment.

Travel expenses.

(2) If an individual who is an officer or employee of the United States Government serves as a member of the Board of Directors or as an officer or employee of the Endowment, that individual may

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not receive any compensation or travel expenses in connection with services performed for the Endowment.

(d)(1) The Endowment shall not issue any shares of stock or

Stock or
dividends.

(2) No part of the assets of the Endowment shall inure to the benefit of any member of the Board, any officer or employee of the Endowment, or any other individual, except as salary or reasonable compensation for services.

(e)(1) The accounts of the Endowment shall be audited annually in accordance with generally accepted auditing standards by independent certified public accountants or independent licensed public accountants certified or licensed by a regulatory authority of a State or other political subdivision of the United States. The audits shall be conducted at the place or places where the accounts of the Endowment are normally kept. All books, accounts, financial records, reports, files, and all other papers, things, or property belonging to or in use by the Endowment and necessary to facilitate the audits shall be made available to the person or persons conducting the audit, and full facilities for verifying transactions with any assets held by depositories, fiscal agents, and custodians shall be afforded to such person or persons.

Audits.

(2) The report of each such independent audit shall be included in the annual report required by subsection (h). The audit report shall set forth the scope of the audit and include such statements as are necessary to present fairly the Endowment's assets and liabilities, surplus or deficit, with an analysis of the changes therein during the year, supplemented in reasonable detail by a statement of the Endowment's income and expenses during the year, and a statement of the application of funds, together with the independent auditor's opinion of those statements.

Report.

(f)(1) The financial transactions of the Endowment for each fiscal year may be audited by the General Accounting Office in accordance with such principles and procedures and under such rules and regulations as may be prescribed by the Comptroller General of the United States. Any such audit shall be conducted at the place or places where accounts of the Endowment are normally kept. The representatives of the General Accounting Office shall have access to all books, accounts, records, reports, files, and all other papers, things, or property belonging to or in use by the Endowment pertaining to its financial transactions and necessary to facilitate the audit; and they shall be afforded full facilities for verifying transactions with any assets held by depositories, fiscal agents, and custodians. All such books, accounts, records, reports, files, papers, and property of the Endowment shall remain in the possession and custody of the Endowment.

GAO audit.

(2) A report of each such audit shall be made by the Comptroller General to the Congress. The report to the Congress shall contain such comments and information as the Comptroller General may deem necessary to inform the Congress of the financial operations and condition of the Endowment, together with such recommendations with respect thereto as he may deem advisable. The report shall also show specifically any program, expenditure, or other financial transaction or undertaking observed in the course of the audit which, in the opinion of the Comptroller General, has been carried on or made contrary to the requirements of this title. A copy of each report shall be furnished to the President and to the Endowment at the time submitted to the Congress.

Report to
Congress.

Report to
President.

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Recordkeeping.

(5)(1) The Endowment shall ensure that each recipient of assistance provided through the Endowment under this title keeps such records as may be reasonably necessary to fully disclose the amount and the disposition by such recipient of the proceeds of such assistance, the total cost of the project or undertaking in connection with which such assistance is given or used, and the amount and nature of that portion of the cost of the project or undertaking supplied by other sources, and such other records as will facilitate an effective audit.

Information accessibility.

(2) The Endowment shall ensure that it, or any of its duly authorized representatives, shall have access for the purpose of audit and examination to any books, documents, papers, and records of the recipient that are pertinent to assistance provided through the Endowment under this title. The Comptroller General of the United States or any of his duly authorized representatives shall also have access thereto for such purpose.

Report to President and Congress.

(h) Not later than December 31 of each year, the Endowment shall submit an annual report for the preceding fiscal year to the President for transmittal to the Congress. The report shall include a comprehensive and detailed report of the Endowment's operations, activities, financial condition, and accomplishments under this title and may include such recommendations as the Endowment deems appropriate. The Board members and officers of the Endowment shall be available to testify before appropriate committees of the Congress with respect to such report, the report of any audit made by the Comptroller General pursuant to subsection (f), or any other matter which any such committee may determine.

Foreign Missions Amendments Act of 1983**TITLE VI—FOREIGN MISSIONS****SHORT TITLE**

22 USC 4301 note.

SEC. 601. This title may be cited as the "Foreign Missions Amendments Act of 1983".

REQUIREMENT FOR LIABILITY INSURANCE

SEC. 602. Section 6 of the Diplomatic Relations Act (22 U.S.C. 254e) is amended—

(1) in subsection (a) by striking out "President" and inserting in lieu thereof "Director of the Office of Foreign Missions in the Department of State";

(2) in subsection (b) by striking out "The President shall, by regulation, establish liability insurance requirements" and inserting in lieu thereof "The Director of the Office of Foreign Missions shall, by regulation, establish liability insurance requirements which can reasonably be expected to afford adequate compensation to victims and which are"; and

(3) in subsection (c) by striking out "President" and inserting in lieu thereof "Director of the Office of Foreign Missions".

ENFORCEMENT OF COMPLIANCE WITH LIABILITY INSURANCE REQUIREMENTS

SEC. 603. Title II of the State Department Basic Authorities Act of 1966 is amended by inserting after section 204 (22 U.S.C. 4304) the following new section:

ALCOHOL AND TOBACCO
DIVERSION AND CONTRABAND
TRAFFICKING



ALCOHOL & TOBACCO PROGRAMS
DIVERSION BRANCH

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OVERVIEW OF TOBACCO CONTRABAND TRAFFICKING

Criminal tobacco trafficking usually occurs when foreign governments or state governments impose a higher excise tax on tobacco products than found in surrounding jurisdictions. These tax disparities lead to large-scale tobacco (cigarette) diversion from a lawful to an unlawful destination, thus defrauding the state or foreign governments of their due revenue.

There has been an over 500% increase from 1992 to present in the number of contraband cigarette trafficking tobacco investigations that ATF is conducting. The recent rise in trafficking is attributable to a number of factors, most notably a significant increase in both Canadian federal and provincial tobacco taxes in the late 1980s/early 1990s and an increase in certain states' cigarette taxes. Intelligence has determined that there exists a network of traditional and nontraditional organized crime groups operating transnationally. ATF is working approximately 65 investigations involving Canadian/U.S. and Mexican/U.S. cigarette trafficking, low-state-to-high-state trafficking, and Native American illegal sales.

Canada's initial tax increase was an attempt to generate health care revenue and to decrease cigarette consumption. The criminal diversion of tobacco products into Canada evolved from small, individual smuggling activities into sophisticated criminal enterprises. Canadian/U.S. criminal organizations have defrauded the Canadian government of between one and two billion dollars in revenue per year. ATF, IRS, US Customs and other Federal agencies recently indicted 21 individuals allegedly involved in Canadian/U.S. alcohol/tobacco

trafficking to Canada. Assets from this illegal activity are estimated at over \$500 million. In a similar scenario, higher state taxes in the Southwest has brought about U.S./Mexican diversion involving U.S. cigarettes "for export only." Export cigarettes are exempt from Federal taxes.

In the low-state-to-high-state trafficking, Michigan shows the greatest loss of state revenue with a conservative estimate of \$75 million per year. Michigan has the third highest cigarette taxes in the U.S. Michigan traffickers obtain illegal cigarettes from wholesalers and retailers located throughout the South, where tobacco is traditionally taxed at a lower rate.

ATF is also working in conjunction with state revenue and law enforcement authorities investigating illegal Native American cigarette sales to non-Native Americans. Native American cigarette tax structure varies by state although the supplier of cigarettes involved in the trafficking have been from out-of-state wholesalers. Smoke shops making illegal tax-free sales in New York, Oklahoma, Arizona, New Mexico, Washington state and Montana have been identified.

ATF is conducting ongoing liaison with other foreign law and revenue enforcement authorities to ascertain the scope of cigarette trafficking worldwide. ATF is also currently working with criminal investigators and tax officials in East European countries to develop tobacco regulations and also establish criminal enforcement in this area. For more information contact Chief, Diversion Branch, (202)927-8210.

Distribution System of Distilled Spirits

The distribution system for distilled spirits is a three-tier system - the distilled spirits plant (DSP) is at the top, a wholesale liquor dealer (WLD), is in the middle, and the bottom tier is the retail liquor dealer (RLD), the retail store from where consumers make their purchases. Except for in the case of exportation, tax is generally due upon removal of the distilled spirits from the DSP.

A WLD is defined as every person who sells, or offers for sale, distilled spirits wines, or beer to another dealer. The WLD must meet the requirements of Federal law by obtaining a basic permit and paying Special Tax. WLDs are required to maintain daily records of receipt and disposition of distilled spirits in accordance with 27 CFR Part 194.

The bottom tier of the three tier system, the RLD, is defined as every person who sells, or offers for sale, distilled spirits, wine, or beer to any person other than a dealer. RLDs are not required to obtain a permit from ATF, however they must pay Special Tax. All RLDs are required by 27 CFR Part 194 to keep records of receipt for all distilled spirits, and records for the disposition of 20 wine gallons or more of distilled spirits. (Distribution of 20 wine gallons or more to an individual constitutes a sale to a dealer. Such individuals are required to have a wholesalers basic permit).

Exportation

Distilled spirits may leave the plant without payment of tax for exportation, provided certain export steps are followed. After submitting the required notice to the appropriate District Director, the spirits may be withdrawn for direct exportation to the foreign customer, or for transfer to a Customs Bonded Warehouse (CBW) or Foreign Trade Zone (FTZ) for subsequent exportation. Upon proof of exportation, the DSP is relieved from the applicable tax liability.

Distribution System of Cigarettes

After the manufacture of cigarettes, the general industry pattern is to ship packaged Federally tax paid tobacco products to public warehouses that serve all manufacturers. There are approximately 81 public warehouses across the country. Public warehouses are not regulated by ATF.

The cigarettes remain the property of the manufacturers while in the public warehouse and are removed only upon the manufacturer's instructions. The cigarettes are distributed to wholesalers (stamping agents), government installations, and other public warehouses in the warehouse's distributing area for subsequent distribution to consumers.

A wholesaler stamping agent (WSA) is defined as a business having the authority from a state to affix to cigarette packs evidence of the appropriate state tax. By affixing tax stamps to cigarettes, the business becomes a licensed agent of that state. The WSA usually sells the cigarettes to other wholesalers (non-stamping agents), subjobbers and retailers.

State tax exempt sales consist primarily of sales to military installations, Veterans Hospitals, and Indian reservations.

Exportation

Tobacco products may be exported tax-free directly from the manufacturer or from export warehouses (EW). Packages of cigarettes destined for exportation are required to be marked with the statement "Tax-exempt. For use outside the U.S." or, "U.S. Tax exempt. For use outside the U.S." The tax liability is relieved once the manufacturer or export warehouse proprietor provides ATF with proof of exportation.

EWs are regulated by ATF, and they are required to obtain a permit, a bond and pay special tax. EWs generally receive tobacco products straight from the manufacturer, however, some are received from other export warehouses. Cigarettes travel in bond to the EW. Once the cigarettes reach the EW, they transfer from the manufacturer's bond to the EW's bond. The EW is now liable for the tax until proof of exportation is submitted or the cigarettes are transferred to another EW's bond.

Cigarettes may also be exported through an FTZ or CBW. Upon entry into the FTZ or CBW the cigarettes are considered to be exported. FTZs and CBWs are under Customs jurisdiction, however ATF may gain access to them with coordination through Customs.

DOMESTIC CIGARETTES

20 CIGARETTES = 1 PACK
25 CIGARETTES = 1 PACK

10 PACKS = 1 CARTON
8 PACKS = 1 CARTON

200 CIGARETTES = 1 CARTON

12,000 CIGARETTES = 1 CASE (12M)* 60 CARTONS = 1 CASE
6,000 CIGARETTES = ½ CASE (6M)

60,000 CIGARETTES = 5/10 THOUSAND STD CASES
6/12 THOUSAND STD CASES
3,000 PACKS
300 CARTONS

EXPORT CIGARETTES

10,000 CIGARETTES = 1 CASE (10M)
5,000 CIGARETTES = ½ CASE (5M)

* 12M/6M or 10M/5M notes markings of how many cigarettes there are per case. However, a case marked 12M/6M or 10M/5M will not necessarily contain 12,000/6,000 or 10,000/5,000 cigarettes, since the cases may be broken up. Individual cartons should be visually verified.

The 5 states that do not tax stamp their cartons are: *Alaska, Hawaii, Michigan, North Carolina and South Carolina.*

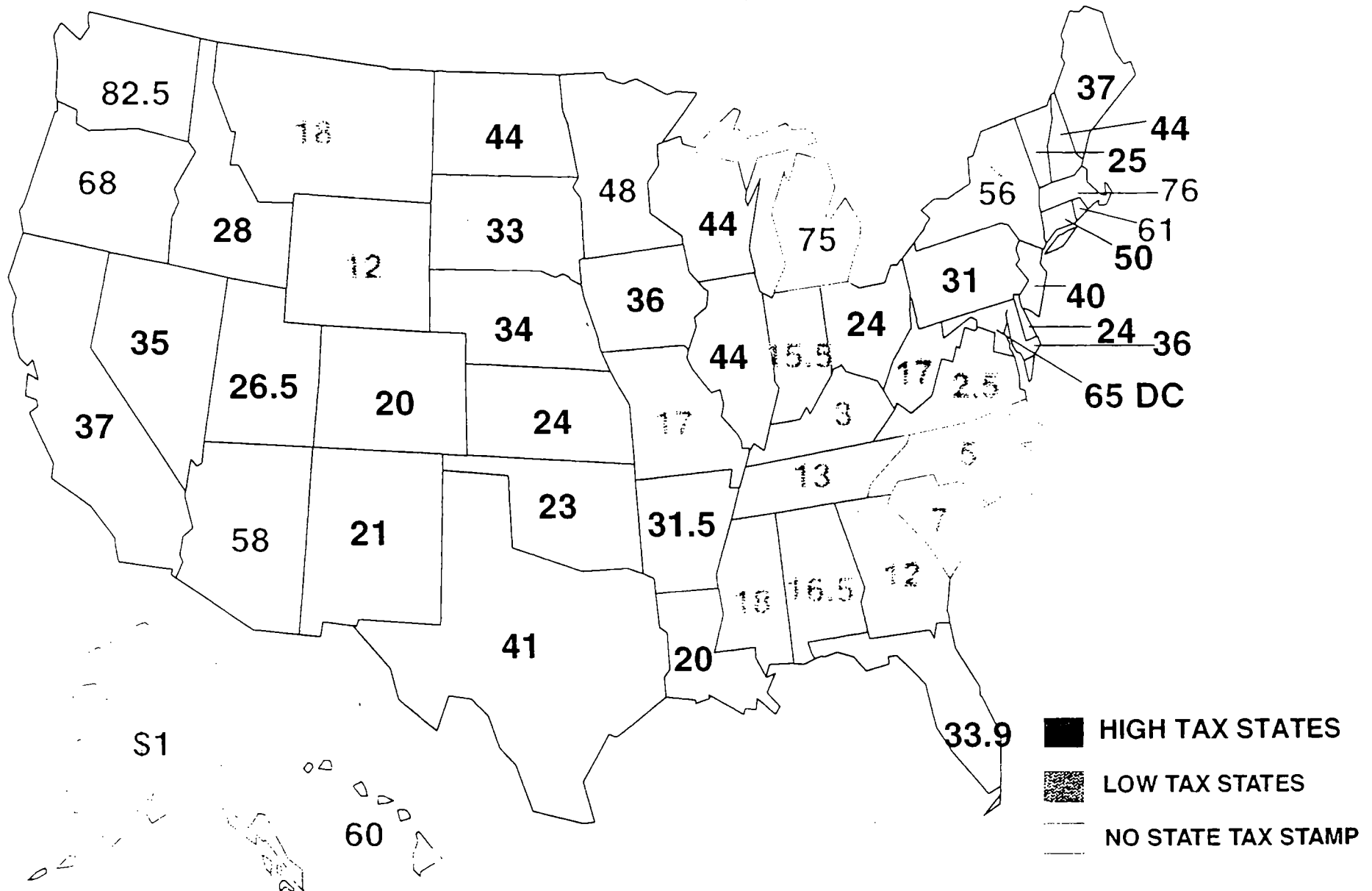
FEDERAL TAX

\$12.00 per 1,000 cigarettes
\$00.24 per pack of 20 cigarettes
\$00.30 per pack of 25 cigarettes

At Least 60,000+ Cigarettes Are Needed for an ATF Criminal Case.

STATE EXCISE TAX RATE ON CIGARETTES

20 CIGARETTE PACK/ IN CENTS



DISTILLED SPIRITS

Federal Tax Rate = \$13.50 per proof gallon

Equivalents of Commonly Diverted Case Sizes

<u>Bottle size</u>	<u>Bottles per case</u>	<u>Liters per case</u>	<u>Proof</u>	<u>Tax Rate/bottle</u>	<u>Tax Rate/case</u>
1 liter	12	12.0	80	\$2.85	\$34.20
1.75 liter	6	10.5	80	\$4.99	\$29.90

DISTILLED SPIRITS

Federal Tax Rate = \$13.50 per proof gallon

Equivalents of Commonly Diverted Case Sizes

<u>Bottle size</u>	<u>Bottles per case</u>	<u>Liters per case</u>	<u>Proof</u>	<u>Tax Rate/bottle</u>	<u>Tax Rate/case</u>
1 liter	12	12.0	80	\$2.85	\$34.20
1.75 liter	6	10.5	80	\$4.99	\$29.90

State Liquor Excise Tax Rates

January 1, 1997

STATE	EXCISE TAX RATES		
	SALES TAXES (\$ per gallon)	APPLIED	OTHER TAXES
Alabama	see footnote (1)	Yes	
Alaska	\$5.60	n.a.	under 21% - \$0.85/gallon
Arizona	3.00	Yes	
Arkansas	2.50	Yes	under 5% - \$0.50/gallon. under 21% - \$1.00/gallon. \$0.20/case and 3% off- 14% on-premise retail taxes
California	3.30	Yes	over 50% - \$6.60/gallon
Colorado	2.28	Yes	
Connecticut	4.50	Yes	under 7% - \$2.05/gallon
Delaware	3.75	n.a.	under 25% - \$2.50/gallon
Florida	6.50	Yes	under 17.259% - \$2.25/gallon. over 55.780% - \$9.53/gallon \$0.10/ounce on-premise retail tax
Georgia	3.79	Yes	\$0.83/gallon local tax
Hawaii	5.87	Yes	
Idaho	see footnote (1)	Yes	
Illinois	2.00	Yes	under 14% - \$0.23/gallon. \$0.50/gallon in Chicago and \$1.00/gallon in Cook County
Indiana	2.68	Yes	under 15% - \$0.47/gallon
Iowa	see footnote (1)	Yes	
Kansas	2.50	no	8% off- and 10% on-premise retail tax
Kentucky	1.92	Yes*	under 6% - \$0.25/gallon. \$0.05/case and 9% wholesale tax
Louisiana	2.50	Yes	under 6% - \$0.32/gallon
Maine	see footnote (1)	Yes	
Maryland	1.50	Yes	
Massachusetts	4.05	Yes*	under 15% - \$1.10/gallon. over 50% alcohol - \$4.05/proof gallon. 0.57% on private club sales
Michigan	see footnote (1)	Yes	
Minnesota	5.03	--	\$0.01/bottle (except miniatures) and 8.5% sales tax
Mississippi	see footnote (1)	Yes	
Missouri	2.00	Yes	
Montana	see footnote (1)	n.a.	
Nebraska	3.00	Yes	

Nevada	2.05	Yes	under 14% - \$0.40 gallon and under 21% - \$0.75 gallon.
New Hampshire	see footnote (1)	n.a.	
New Jersey	4.40	Yes	
New Mexico	6.06	Yes	
New York	6.44	Yes	under 24% - \$2.54/gallon; \$1.00/gallon New York City
North Carolina	see footnote (1)	Yes*	
North Dakota	2.50	--	7% state sales tax
Ohio	see footnote (1)	Yes	
Oklahoma	5.56	Yes	\$1.00/bottle on-premise and 12% on-premise
Oregon	see footnote (1)	n.a.	
Pennsylvania	see footnote (1)	Yes	
Rhode Island	3.75	Yes	
South Carolina	2.72	Yes	\$5.36/case and 9% surtax
South Dakota	3.93	Yes	under 14% - \$0.93/gallon; 2% wholesale tax
Tennessee	4.00	Yes	\$0.15/case and 15% on-premise; under 7% - \$1.10/gallon.
Texas	2.40	Yes	14% on-premise and \$0.05/drink on airline sales
Utah	see footnote (1)	Yes	
Vermont	see footnote (1)	no	
Virginia	see footnote (1)	Yes	
Washington	see footnote (1)	Yes*	
West Virginia	see footnote (1)	Yes	
Wisconsin	3.25	Yes	
Wyoming	see footnote (1)	Yes	
Dist. of Columbia	1.50	Yes	8% off- and 9% on-premise sales tax
U.S. Median	\$3.25		

Source: Compiled by FTA from various sources.

* Sales tax is applied to on-premise sales only.

(1) In 18 states, the government directly controls the sales of distilled spirits. Revenue in these states is generated from various taxes, fees and net liquor profits.

EXISTING CONTROLS FOR THE ALCOHOL & TOBACCO INDUSTRIES UNDER CURRENT LAW

ALCOHOL

TYPE OF INDUSTRY	DISTILLED SPIRITS PLANT	WHOLESALE AND/OR IMPORTER	RETAILER
DOCUMENTS REQUIRED:			
APPLICATION - FAA	YES	YES	NO
APPLICATION - IRC	YES	NO	NO
BOND(S)	YES	NO	NO
CORPORATE CHARTER OR CERTIFICATE	YES	YES	NO
LIST OF OFFICERS AND DIRECTORS	YES	YES	NO
PERSONNEL QUESTIONNAIRES	YES	YES	NO
LIST OF PERSONS HOLDING MORE THAN 10% STOCK	YES	YES	NO
TRADE NAME REGISTRATION	YES	YES	NO
APPLICANT RECEIVES:			
BASIC PERMIT - FAA	YES*	YES	NO
IRC PERMIT	YES*	NO	NO
APPROVED REGISTRATION	YES	NO	NO
STATE LICENSE/PERMIT	YES	YES	YES
SPECIAL OCCUPATIONAL TAX (SOT)	YES	YES	YES
RECORDS:			
MONTHLY REPORT OF OPERATIONS	YES	NO	NO
RECORDS OF RECEIPT	YES	YES	YES
RECORDS OF DISPOSITION	YES	YES	YES***

TOBACCO

TOBACCO PRODUCTS MANUFACTURER	EXPORT WAREHOUSE PROPRIETOR	WHOLESALE AND/OR IMPORTER**	RETAILER
N/A	N/A	N/A	N/A
YES	YES	NO	NO
YES	YES	NO	NO
YES	YES	NO	NO
YES	YES	NO	NO
YES	YES	NO	NO
N/A	N/A	N/A	N/A
YES	YES	NO	NO
NO	NO	NO	NO
YES	YES	YES	YES
YES	YES	NO	NO
YES	YES	NO	NO
YES	YES	NO	NO
YES	YES	YES***	YES***

* DEPENDING UPON PROPOSED ACTIVITIES

** WILL NEED AN IMPORTER'S PERMIT BY YEAR 2000

*** IF MORE THAN 20 WINE GALLONS FOR ALCOHOL/ MORE THAN 60,000 CIGARETTES FOR TOBACCO

- a. reasonably foreseeable
- b. in furtherance of
- c. original conspiracy
- d. committed while the person is a part of the conspiracy

18 U.S.C. § 1001

False statements in matters within jurisdiction of any department or agency of U.S.

IRC TAX VIOLATIONS ON NON-UNITED STATES TAX PAID LIQUOR

26 U.S.C. § 5601(a)
(1) - (a) (15)

Penalties for unlawful warehousing, processing, withdrawal distilling purchase of distilled spirits, etc. include up to 5 years imprisonment and/or \$10,000 fine

26 U.S.C. § 5602

Penalties for tax fraud by distiller-Up to 5 years imprisonment and/or \$10,000 fine

26 U.S.C. § 5603

Penalties for fraudulent violations of IRC recordkeeping requirements-up to 5 years imprisonment or \$10,000 fine

26 U.S.C. § 5691(a) -
Willful failure to pay
special occupational tax
as a wholesaler.
Punishable by up to 2
years in prison

26 U.S.C. § 7201
Willful intent to evade
or defeat tax. Penalty-
Up to 5 years
imprisonment/fine up to
\$100,000 (\$500,000 fine
if corporation

26 U.S.C. § 7206
Fraud and false statements

Penalty-Up to 3 years
imprisonment and/or
\$100,000 fine. \$500,000
fine in the case of a
corporation

26 U.S.C. § 5762

Criminal penalties
associated with failing
to comply with Internal
Revenue law relating to
taxes, records and
permits for manufacturers
and exporters of tobacco
products

18 U.S.C. § 1263

Anyone who ships distilled spirits
in United States must have a bill
of lading accompanying shipment
accurately showing contents of
shipment and consignee.

IV. Regulatory Issues
Alcohol/Diversion

A. Tax Cases

Distilleries must document the exportation of liquors.

ATF's position set forth in Industry Circular 94-1 dated 4/14/94.

26 U.S.C. § 5001 imposes tax on all distilled spirits.

26 U.S.C. § 5111 requires wholesalers to pay \$500/yr. special (occupational) tax. The penalty for willful failure to pay SOT is \$5,000/2 yrs.

26 U.S.C. § 5214(a)(4) allows distilled spirits to be removed without payment of tax after filing bonds required by 26 U.S.C. § 5175 and complying with ATF regulations.

26 U.S.C. § 5005, proprietor is liable for tax of spirits produced on the bonded premises of DSP.

Relief from liability only occurs when export occurs pursuant to 26 U.S.C. § 5005(e) and distillery provides proof of export. ATF regulations specify certain proof of export. See 27 C.F.R. §§ 252.40 and 252.250-269.

B. Documenting Alcohol Diversion
Tax Cases

1. Establish that the proof of export is inadequate
2. Establish false bills of lading or false ATF Form 5100.11

C. Administrative Liability
(Tax Paid Alcohol Cases)

Establish violation of conditions of basic permit (violation of 27 U.S.C. § 204(d)) due to:

1. 18 U.S.C. § 1154(a) and 1156 illegal shipments of liquor and/or illegal possession into Indian Country. (Discussed in detail in Indian section)

2. Shipments of distilled spirits into state in violation of State law is a violation of Webb-Kenyon statute, 27 U.S.C. § 122, as well as 21st Amendment.

3. ATF Industry Circular 1995-1 (1/19/95) discusses liability as principal or aider and abettor for violations of Internal Revenue Code, FAA Act, Webb-Kenyon, and Indian provisions

VI. State and Local Law Issues

The Webb-Kenyon Act, 27 U.S.C. § 122, a statutory declaration of the twenty-first amendment, provides that the shipment of alcoholic beverages from one State into any other State in violation of the laws of the receiving State is prohibited.

Neither the twenty-first amendment nor Webb-Kenyon provide for any criminal or civil penalties for violations thereof.

The Federal Alcohol Administration Act (FAA Act), 27 U.S.C.

§ 203, requires a basic permit in order to engage in the business of importing alcoholic beverages, distilling distilled spirits or producing wine. Finally, persons who engage in the business of purchasing for resale at wholesale distilled spirits, wine, or malt beverages must obtain basic permits.

27 U.S.C. § 204(d) provides that basic permits are conditioned upon compliance with the twenty-first amendment and the laws relating to its enforcement. As such, violation of either the twenty-first amendment or Webb-Kenyon arising from violations of State law either directly or as an aider or abettor could result in the suspension or revocation of the basic permit of the violator.

VIII. Tobacco Diversion and Regulatory Requirements

Introduction

Criminals engage in tobacco diversion for the same reason as alcohol diversion. They make profits by transporting cigarettes from low tax jurisdictions to high tax jurisdictions and from regulated channels to unregulated channels.

Cigarettes are diverted from low tax jurisdictions like North Carolina and Virginia to high tax jurisdictions like New York, Michigan, Washington, and from the U.S. to Canada.

Cigarettes are diverted from alleged export to the U.S. market by filing false paperwork at FTZ's, CBW's, and export warehouses, wherein goods are allegedly exported but in fact stay in the United States. Cigarettes are smuggled into the United States from other countries, including Canada and Mexico.

A. CONTRABAND CIGARETTE
TRAFFICKING ACT (CCTA) (18 U.S.C. §
2341 et seq.)

Makes it unlawful for any person to ship, transport, receive, possess, sell, distribute or purchase in excess of 60,000 cigarettes which bear no evidence of State tax payment in State in which cigarettes are

found, if such State requires a stamp to evidence payment of taxes.

Elements of CCTA Act violation

1. Defendant shipped, transported, received, possessed, sold, distributed or purchased cigarettes without the requisite tax stamps;
2. Quantity of cigarettes exceeded 60,000 cigarettes, i.e. more than 5 cases of cigarettes
3. The State required a tax stamp.
4. CCTA applies to shipments over 5 cases. United States v. DiMaria, 727 F.2d 265 (2nd Cir. 1984). 60,000 cigarettes must be transported to fall within scope of CCTA. U.S. v. Paradiso, 689 F.2d 28 (2nd Cir. 1982).

Penalties-Up to 30 years imprisonment or fines.

5. ATF takes the position that the Contraband Cigarette Act applies to Indian tribes. CC Case No. 41,112, 10/9/92. U.S. v. Baker, 63 F.3d 1478 (9th Cir. 1995), cert. denied 116 S.Ct. 824 (1996) (Indians are not exempt from CCTA and Washington State tax is valid to Indians); U.S. v. Gord, 77 F.3d 1192 (9th Cir. 1996) (Unstamped cigarettes which were not pre-approved by Washington State Dept. of Revenue for resale to Indians were contraband under CCTA even if smokeshop were tribal organization and distributes cigarettes to only Native Americans).

6. While the regulations do not preclude a distributor from dividing a single agreement for the disposition of more than 60,000 cigarettes or less, the distributor must record the required information for each component of the agreement. T.D. ATF-73, 45 Fed. Reg. 18609, July 21, 1980. A distributor who fails to keep the required records for each component of an agreement for the disposition of more than 60,000 cigarettes would be in violation of the regulations.

Thus, even where a defendant does not have actual possession of more than 60,000 cigarettes, it may be possible to establish that such defendant has constructive possession of such a quantity of cigarettes because such defendant has the power and intention at a given time to exercise dominion and control over the cigarettes, either directly or through others.

Given this stated purpose, any interpretation of the law that would categorically allow organized crime and large scale operators to circumvent its scope by merely splitting shipments would allow such persons to operate with virtual impunity, a situation which cannot be tolerated. See Id. at 5524.

9. CCTA can be used in conjunction with wire, mail fraud, money laundering, and RICO statutes. U.S. v. Baker (Paragraph 5) (CCTA violation resulted in RICO case and million dollar forfeiture using the aforementioned statutes)

B. JENKINS ACT (15 U.S.C. § 375)
Any person who sells cigarettes in interstate commerce when the cigarettes are transported into a State taxing their sale to other than a licensed distributor must:
(1) first file w/State tobacco tax administrator their name and place of business and (2) by the 10th of each calendar month an invoice detailing shipments made into the State during the previous month including purchaser, brand, and quantity.

7. Where a distributor effects multiple agreements for the disposition of cigarettes which if executed singly would exceed 60,000 in quantity in order to avoid the purview of the regulations, a determination as to whether such distributor is nevertheless covered by the regulations must be made upon the facts of the particular case. As stated in T.D. ATF-73, it is impossible to provide a general statement or definition as to what constitutes evidence of a distributor's intent to avoid the requirements of this regulation outside the context of a particular case. 45 Fed. Reg. 18612.

8. Similarly, it is not possible to provide a general statement as to whether a person is in violation of section 2342(a) where such person divides quantities of more than 60,000 cigarettes into smaller components in order to avoid the purview of the law. However, since the term contraband cigarettes is defined to require "possession" of greater than 60,000 cigarettes, it may be possible to establish a violation of section 2342 under the doctrine of constructive possession, depending upon the facts of a particular case.

CIGARETTE HOTLINE INTAKE REPORT

HOTLINE NUMBER 97- 1-800-659-6242

CALLER'S NAME: _____
PHONE NUMBER: _____
ORGANIZATION: _____
POSITION: _____

INCIDENT DATA

INCIDENT: _____

DATE: _____ TIME: _____
LOCATION: _____
DESCRIPTION: _____

AMOUNT: _____
PRINTED CODING/MARKINGS/OTHER IDENTIFICATION: _____

CONTAINER/TRAILER NUMBERS: _____

OTHER: _____

INDIVIDUAL OR BUSINESS IN POSSESSION: _____

ADDRESS OF POSSESSOR: _____

IF KNOWN, ORIGINAL SOURCE OF CIGARETTES: _____
CIRCUMSTANCES: _____

HAS ATF LAW ENFORCEMENT BEEN NOTIFIED? _____(Y) _____(N)

WERE OTHER AGENCIES NOTIFIED? _____(Y) _____(N)

AGENCY: _____

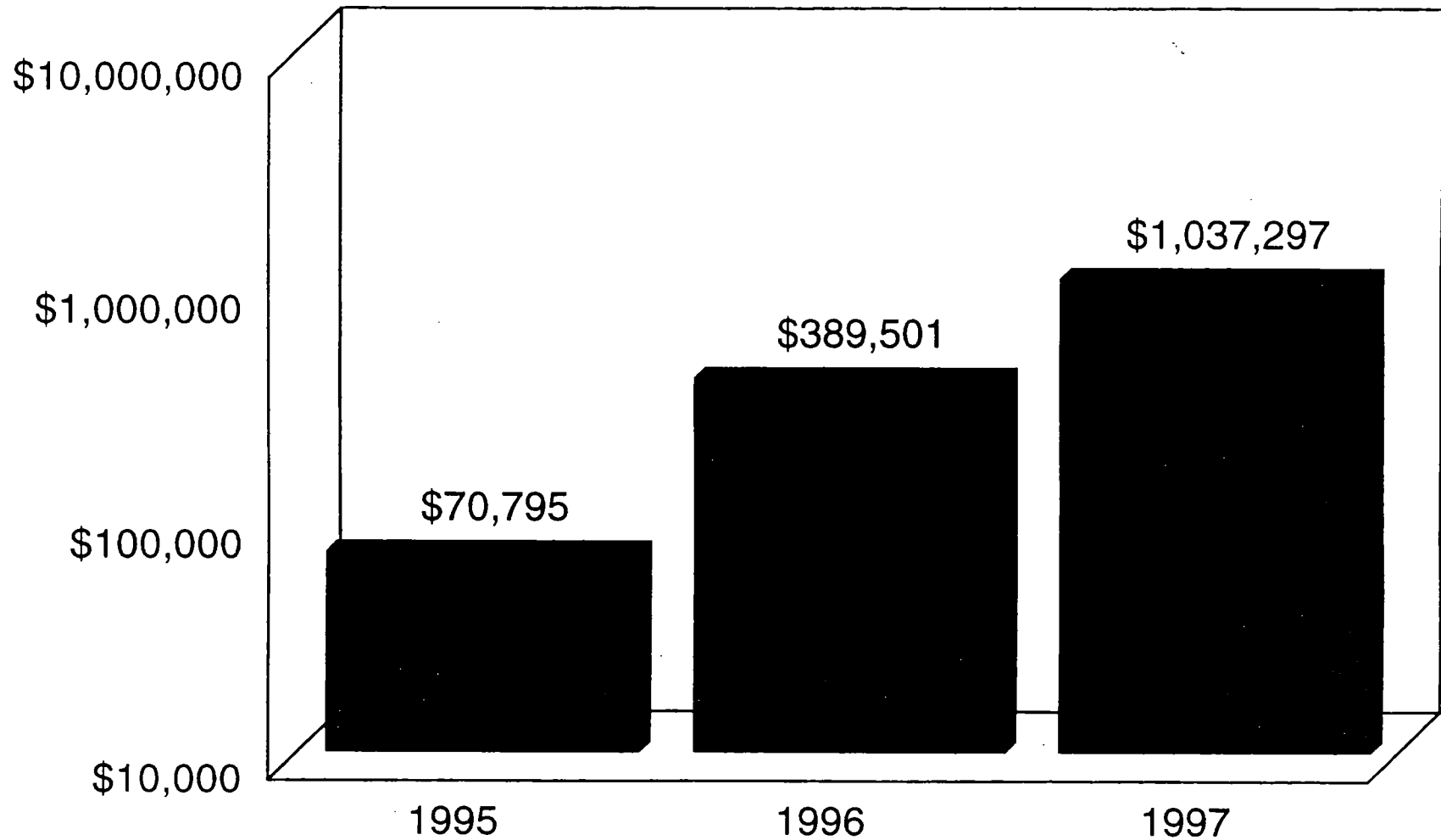
AGENCY REPORT NUMBER: _____

AGENT/INSPECTOR'S NAME: _____

TAKEN BY: _____ TIME: _____

TOBACCO SEIZURES IN DOLLARS

FROM FY 1995-1997



VIOLATIONS

IRC

FAA

**COMMERCE WITH
NATIVE
AMERICANS**

**MONEY
LAUNDERING
CONSPIRACY**



VIOLATIONS



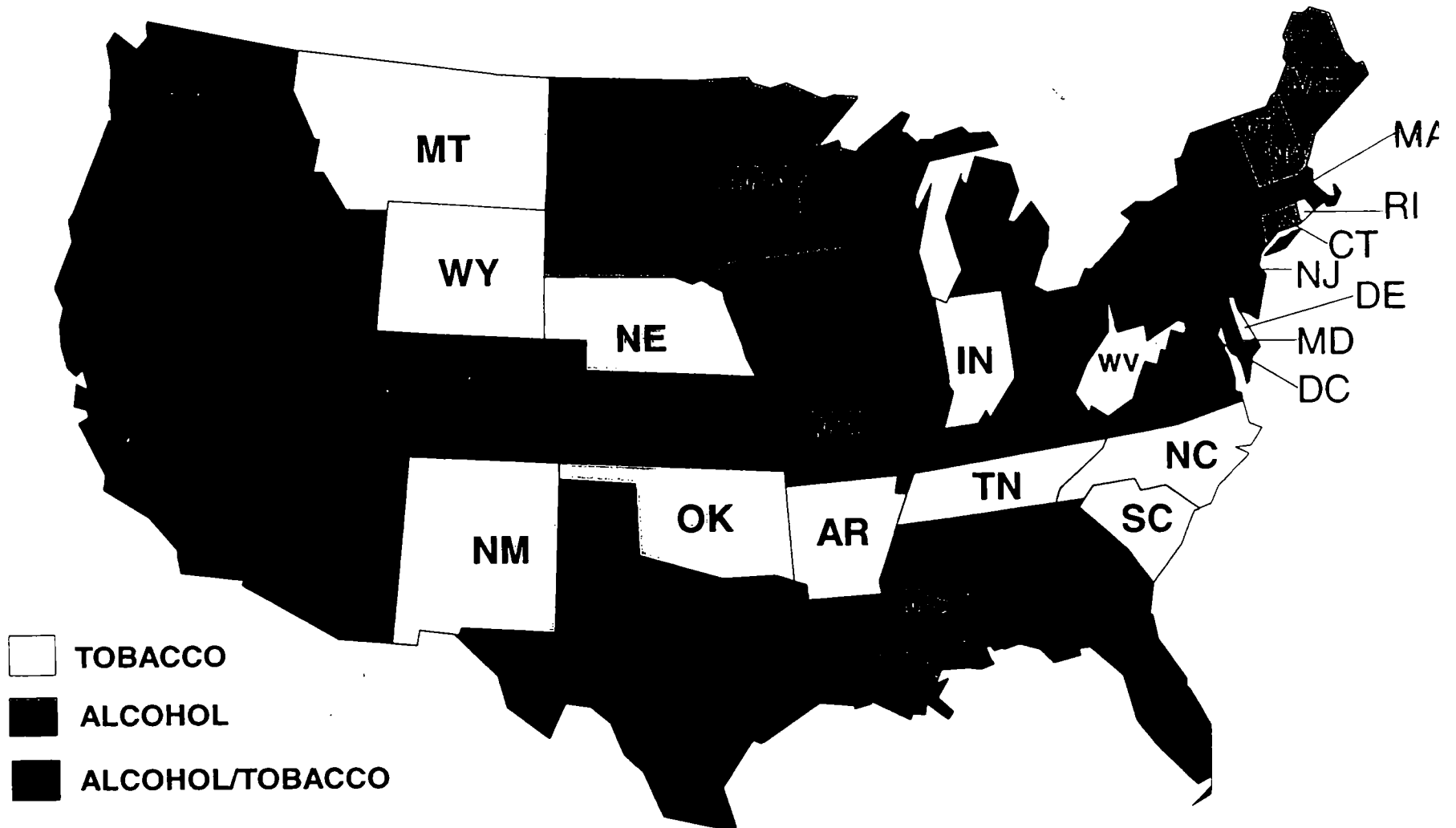
ITAR

CCTA

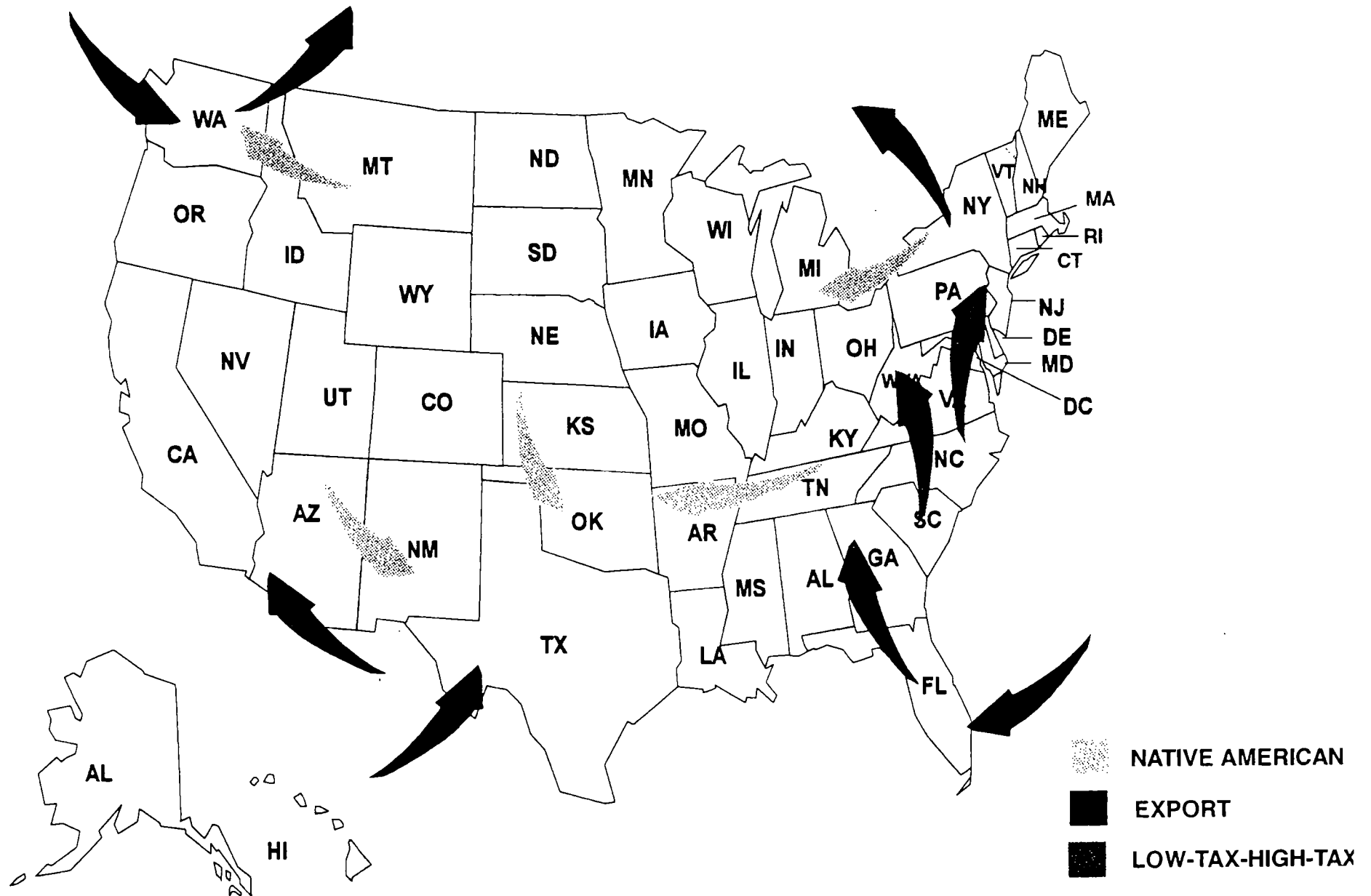
RICO

**WIRE/MAIL
FRAUD**

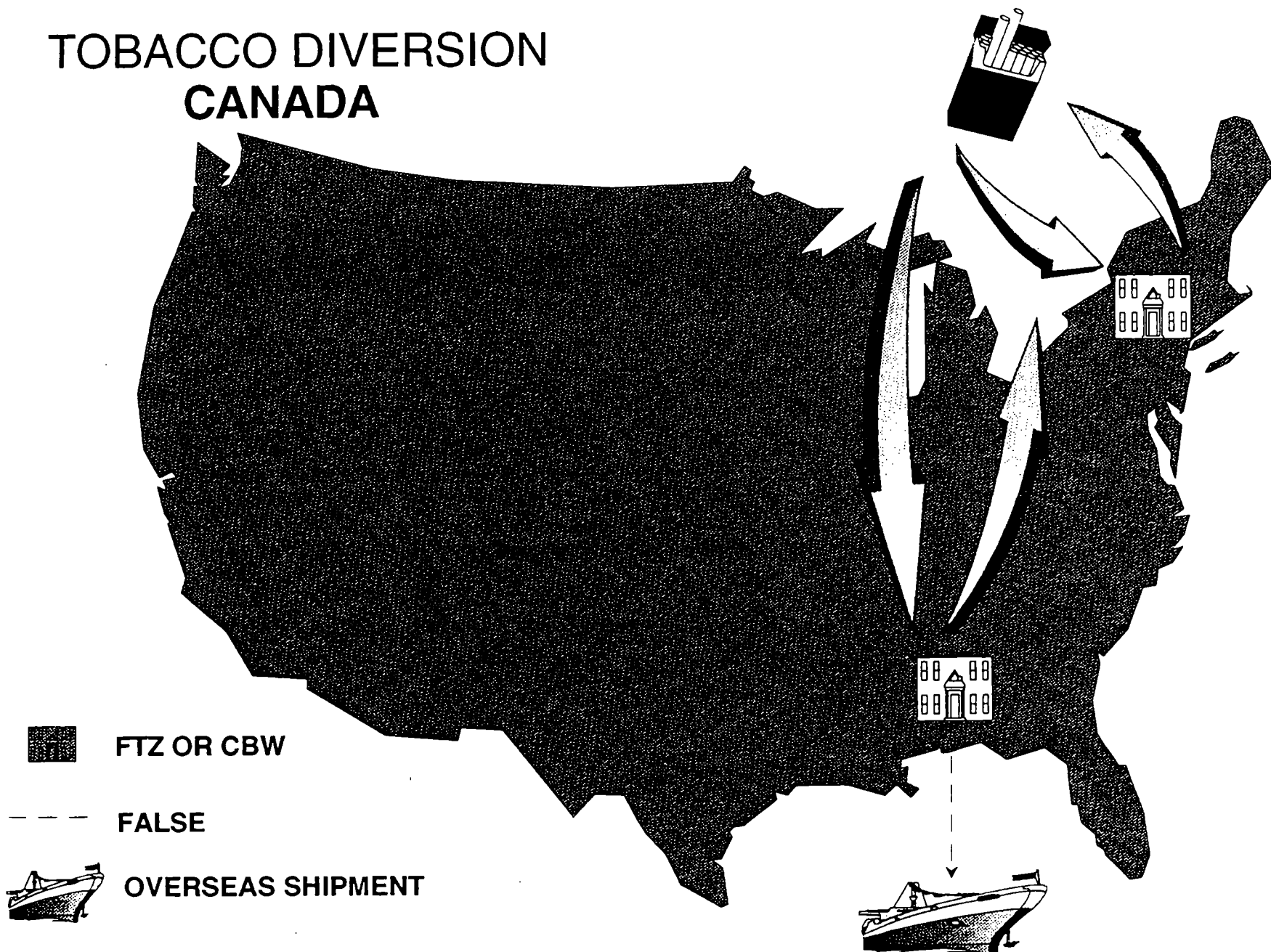
STATES WITH A&T DIVERSION & CONTRABAND ACTIVITIES 1993-1997



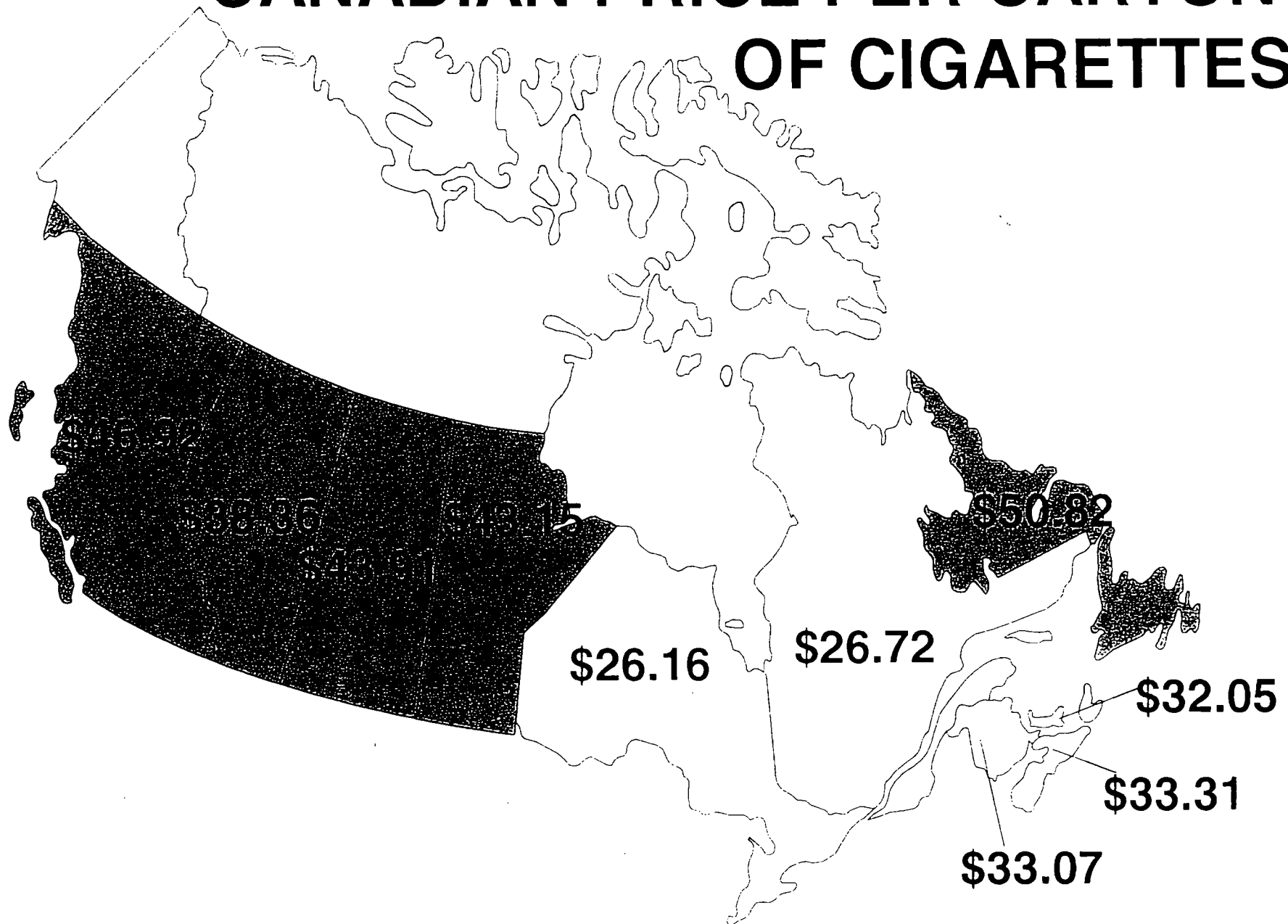
U.S. DIVERSION & CONTRABAND TRAFFICKING ACTIVITY



TOBACCO DIVERSION CANADA



CANADIAN PRICE PER CARTON OF CIGARETTES



MICHIGAN

EST \$50 M PER YEAR LOSS

4TH HIGHEST STATE TAX

NO TAX STAMP ON PACKS

**INVOLVES MAINLY MIDDLE
EASTERN OC**

OBTAIN CIGARETTES FROM

LOW TAX STATES

NY INDIAN RESERVATIONS

WASHINGTON

- LOSES APPROX \$100 M PER YEAR**
- 2ND HIGHEST STATE CIGARETTE TAX**
- NON-COMPLIANCE**
 - 60% FROM WA INDIAN RESERVATIONS**
 - 11% FROM MILITARY BASES**
 - 29% FROM CROSS BORDER SHOPPERS, MAIL ORDER AND EXPORT SCHEMES**

CALIFORNIA

- LOSES APPROX \$30 M PER YEAR
- SOURCE IS PRIMARILY "EXPORTS" TO MEXICO
- MAIN BLACK MARKET SITE IS IN LA
- INVOLVES DIFFERENT CRIMINAL GROUPS

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The Detroit News

July 22, 1997, Tuesday

SECTION: Business; Pg. Pg. B1

LENGTH: 558 words

HEADLINE: Cigarette taxes force smokers to cross borders in search of deals

BYLINE: By Kathy Kristof

BODY:

When Michigan hiked its cigarette excise tax by 50 cents to 75 cents per pack in 1994, taxable cigarette sales plunged 21 percent. But, sales in neighboring Indiana rose 8.5 percent.

California, MASSACHUSETTS, Michigan and New York, with combined populations of 65.4 million and an average cigarette excise tax of 55 cents per pack, reported fewer taxable cigarette sales than the states of Indiana, Kentucky, Missouri, New Hampshire, North Carolina, Tennessee and Virginia, which host half the population and average excise taxes of just 12 cents.

New Hampshire sold twice as many packs of cigarettes as MASSACHUSETTS, even though the rate of smoking in both states is nearly identical. The difference: MASSACHUSETTS has a 76-cent per-pack excise tax, while New Hampshire's excise tax is just 25 cents per pack.

Facts like that amount to a guilty little secret for people like Warren. Once every few weeks, the Washington, D.C., native zips across the Virginia border and loads up on cigarettes. Because cigarette taxes amount to 65 cents per pack in D.C., but less than 3 cents a package in Virginia, he can buy three packs for the price of two.

With a pack-a-day habit -- and a host of chain-smoking friends -- Warren's modest bout into the world of cigarette smuggling saves him a small fortune.

He's not alone. The growing disparity in state cigarette excise tax rates has led to a dramatic increase in both large-scale interstate smuggling and simple "cross-border sales" like Warren's. Although it is not illegal to buy cigarettes

in Virginia and smoke them elsewhere, smuggling for profit is. Moreover, some states limit the number of excise taxable items that come in. Warren asked that his name not be used in print because he doesn't want to explain his trunk full of smokes if it is ever stopped by the authorities.

"I don't think I'm actually breaking the law," he says. "But I may be stretching it."

Cross-border cigarette shopping soared 395 percent between 1980 and 1994 as the state-by-state disparity in cigarette excise taxes widened, according to the Tax Foundation, a Washington, D.C.-based tax research organization. Full-scale cigarette smuggling -- the type done for profit with semi-trucks -- rose a tidy 253 percent during the same period, according to the tax research group.

While tax rates on cigarettes have varied for years, these differences have widened substantially in the past several years and appear to be widening even still. That's mainly because when state budgets began to get squeezed earlier this decade, a host of states opted to boost their revenues by taxing "sin."

Or, at least, unpopular habits, like smoking, drinking and driving a lot. As a result, excise taxes on cigarettes began to soar in some states, where in other states where tobacco lobbies were stronger, they held pat.

Meanwhile, Indian reservations, where Native American tribes are able to sell goods tax-free, have become a haven for mid-state smokers in high-tax states. In Washington, for example, cigarette sales on reservations are believed to account for 14 percent of all cigarettes sold in the state.

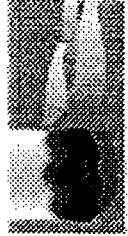
Syndicated columnist Kathy Kristof appears regularly in The Detroit News Business section. Contact her through the Internet at kristof@news.latimes.com. Distributed by Los Angeles Times Syndicate.

LOAD-DATE: July 22, 1997

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Thursday, April 24, 1997

Multistate probe of contraband yields indictments *Cigarettes were trucked to New York*

BY TOM CAMPBELL
Times-Dispatch Staff Writer

A federal and state crackdown on a cigarette-smuggling operation that cheated Virginia and three other states out of \$18 million in tobacco and sales taxes has produced 30 federal indictments, U.S. prosecutors announced yesterday.

The investigation that grew into a multistate, multiagency investigation of the smuggling of cigarettes out of Virginia is expected to produce at least 30 more indictments.

Helen F. Fahey, U.S. attorney for Eastern Virginia, and law enforcement officials from Virginia, New York, Maryland and Pennsylvania announced "Operation Butt-Out" in a news conference yesterday.

The indictments include individuals as well as corporations formed specifically to gain wholesale licenses to obtain the cigarettes to smuggle, authorities said.

Smugglers typically buy cigarettes wholesale at Virginia outlets -- including Sam's Club and Price Club -- drive them to New York City without paying taxes and sell them to buyers there. The Virginia wholesalers do nothing illegal by making such sales, authorities said. They have cooperated fully in the investigation.

"Virginia being a tobacco state and a low-tax state is what makes it attractive," said Bruce Knowlton of the Virginia Alcoholic Beverage Control Board investigations unit.

ABC is part of the 2-year-old smuggling investigation because some of the early targets of the probe held ABC licenses, said Anne Petera, chairman of the ABC Board.

According to law enforcement estimates, smugglers pay an average of \$12.29 per carton in Virginia and typically buy a truckload of about 1,000 cartons per run. They sell them at \$16 a carton to a New York connection for a profit of \$3,710.

The connection sells them, through small stores or bars, for \$21.50 -- still less than the legitimate New York price for cigarettes, with all taxes paid. The connection makes about \$5,500 per truckload.

"The average smuggler will do three loads a week," Knowlton said. He said 10 to 15 smugglers have been operating in and out of Virginia during a typical week, and sometimes that many per day.

Knowlton said the estimated yearly loss in tax revenue from Virginia-to-New York City cigarette smuggling operations is \$16.27 million.

That's about \$1.3 million to Virginia, about \$13 million to New York State and about \$1.8 million to New York City, which imposes its own cigarette tax on top of the state's tax.

"The biggest loser is the state of New York," Knowlton said.

Robert L. Shepherd, deputy commissioner of the New York State Office of Tax Enforcement, attended the news conference.

"It's a multimillion dollar problem," Shepherd said. "And it's mostly our problem, but it's refreshing to see all the agencies involved, state and federal, working so effectively together."

Many of those indicted so far are recent immigrants from the Middle East and Asia, with connections in New York but living in Virginia.

Sometimes only customers known to the retailer get the smuggled cartons, which carry counterfeit tax stamps or none at all. Sometimes they sell to anyone.

"Sometimes the customers know they've gotten bootleg cigarettes," Shepherd said. "Sometimes they don't. Sometimes they don't care."

Assistant U.S. Attorney David Schiller of the Richmond office said the list of indictments covers six conspiracy groups and a few individuals.

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Glossary

Broker - A person who negotiates contracts of purchase and sale.

Carrier - Any person, company, corporation, or organization including a proprietor, owner, consignor, or consignee who transports distilled spirits, denatured spirits, or wine in any manor for himself or others.

Customs Bonded Warehouse (CBW): A building or other secured area under Customs' control in which dutiable goods for export or import may be stored, manipulated, or undergo manufacturing operations without payment of duty. Goods can only move between two CBW's; more than two movements among CBW's requires that the duty be paid.

Consignee - Person to whom goods have been transferred or shipped.

Consignor - The person transferring goods.

Contraband Cigarettes (CCTA)- The possession, transportation, receipt, or shipment of any quantity of cigarettes in excess of 60,000 not bearing the required tax indication of the State in which they are found is prohibited. Tobacco manufacturers, tobacco exporters, common carriers transporting cigarettes under bills of lading and State stamping agents are exempt.

DAG-71 - A Department of Justice form utilized to request a share of property Federally forfeited by a Justice agency (i.e., FBI, DEA, INS). Any Federal, State, or local law enforcement agency that directly participates in an investigation or prosecution that results in a Federal forfeiture may request an equitable share of the net proceeds of the forfeiture.

Detention - Process which enables alcohol products to be held pending determination of tax status.

Distilled Spirits Plant (DSP) - an establishment qualified for distilling, warehousing, processing or any combination thereof.

Diversion - the rerouting of a good or commodity from a legal course to an illegal course.

Electronic fund transfer (EFT): Any transfer of funds effected by a person's financial institution.

Export Warehouse (EW): A bonded internal revenue warehouse for the storage of tobacco products and cigarette papers and tubes, upon which internal revenue tax has not been paid, for subsequent shipment to a foreign country, or for consumption beyond the jurisdiction of the internal revenue laws of the United States.

FAA ACT - The Federal Alcohol Administration Act is the law which provides for the issuance of basic permits to distillers, wholesalers and importers.

Freight Forwarder - A person who arranges the best price, by air, truck, rail or ocean for their client's export shipments.

Foreign Trade Zone (FTZ) - Also known as **Free Trade Zone**. A defined area, outside the Customs territory of the United States, where operations involving foreign and domestic merchandise can take place without being subject (under certain circumstances) to the US customs laws or the payment of duty or tax. Merchandise may be exported, imported, destroyed, or sent into Customs territory from the zone. Cargo can be shuffled among FTZ's until export.

Importer - Any person who brings distilled spirits, wine, beer or tobacco products into the United States.

Internal Revenue Code (IRC) - Contains the Federal laws governing the production and taxation of alcohol and tobacco products.

Non Vessel Operating Commercial Carrier (NVOCC) - leased space available for exported commodities on a passenger ship or steamship line. Potential means of diversion in that the NVOCC can reroute cargo, manipulate cargo or substitute cargo on the dock without the knowledge or consent of DSP, manufacturer or freight forwarder. The cargo container could then still show up as loaded aboard the line.

Retail Liquor Dealer (RLD) - Any person who sells or offers for sale distilled spirits, wine, or beer to any person other than a dealer.

Special Occupational Tax (SOT) also referred to as **Special Tax** - A special tax is imposed by the Internal Revenue Code on persons engaged in certain trades or businesses. Such business includes distilled spirits plants, importers, wholesalers, retail liquor dealers, manufacturers of tobacco products and export warehouses.

Tax determined - Term means that taxable quantities of articles subject to tax have been established.

Tax Free - Term refers to the exemption of Federal taxes on commodities to be exported. Also refers to commodities, such as alcohol and tobacco, that is used for consumption on international shipping vessels.

Tax paid - Term means that all applicable taxes imposed by law have been determined or paid as provided by law.

TD F 92-22-46 - A Department of Treasury form utilized to request a share of property Federally forfeited by a Treasury agency (i.e., US Customs, IRS, ATF or U.S. Secret Service). Any Federal, State, or local law enforcement agency, as well as foreign countries, that directly or indirectly participated in an investigation or prosecution that results in a Federal forfeiture by a Treasury agency may request an equitable share of the net proceeds of the forfeiture. Similar in function to the Department of Justice form, **DAG-71**.

Trafficking - to carry on, trade or deal in the illegal trade of a commodity. Under the CCTA this includes the movement of goods illegally across state lines.

Wholesale liquor dealer: A person who sells or offers for sale distilled spirits, wine or beer to another dealer. A retailer who sales more than 20 gallons of liquor at one time, under Federal law, acts as a wholesaler.