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## Illicit Cigarette Trafficking and the Funding of Terrorism

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Since the dawn of terrorism, procuring finances sufficient to sustain terror operations has been a priority for terrorists. The illicit sale of cigarettes and other commodities by terrorist groups and their supporters has become a crucial part of their funding activities.

Raising the tax on cigarettes widens the difference between the wholesale price and the retail price of the product and inadvertently creates opportunity for traffickers, who evade the tax and gain the profits. Today cigarette traffickers can make as much as \$60 per carton of cigarettes sold illicitly.

Because of the immense profits in the illicit cigarette trade, as well as the potentially low penalties for getting caught, illicit cigarette trafficking now rivals drug trafficking as the method of choice to fill the bank accounts of terrorists and terrorist groups. Investigators have discovered that traffickers in the United States and the United Kingdom are providing material support to the Hezbollah and the Real IRA (RIRA), among other terrorist groups. In addition, law enforcement research indicates that groups tied to al Qaeda, Hamas, PKK (the Kurdish Workers Party), and Islamic Jihad (both Egyptian and Palestinian) are involved in the illicit trafficking of cigarettes.

### Background and History

The trafficking of cigarettes by terrorists and their sympathizers has been going on worldwide since the mid-1990s, and the last four years have seen a sudden increase in trafficking. The trafficking schemes provide the terrorist groups with millions of dollars annually, which fund the purchasing of firearms and explosives to use against the United States, its allies, and other targets.



Authentic Michigan Cigarette Tax Stamps intercepted en route between Beirut, Lebanon,

Investigations have revealed that the terrorist groups work with organized crime groups as well as with the international drug trafficking organizations. Organized crime and drug trafficking organizations already have established trafficking routes, as well as business contacts for the transfer of the commodity for profit. The Bureau of Alcohol, Tobacco, Firearms, and Explosives (ATF) have found that Russian, Armenian, Ukrainian, Chinese, Taiwanese, and Middle Eastern (mainly Pakistani, Lebanese, and Syrian) organized crime groups are highly involved in the trafficking of contraband and counterfeit cigarettes and counterfeit tax stamps for profit.

and Ciudad del Este, Paraguay. Stamps were being sent to Paraguay to be counterfeited. Both the sender of the Stamps and the receiver are believed to have Hezbollah connections.

Known and suspected Hezbollah and Hamas members have established front companies and legitimate businesses in the cigarette trade in Central and South

America. Indications from law enforcement sources are that these companies traffic in contraband and counterfeit cigarettes and tax stamps for profit and then use the proceeds to purchase arms and ammunition.

Using consumables, specifically cigarettes and gasoline, groups that are funding terrorism not only place a legal commodity into an illegal market system but also commit money laundering, fraud (both consumer and business), and tax evasion. The key is that these traffickers are not using the illicitly obtained funds for personal gain but are actually providing the funds as direct support to specific groups that espouse their political or ideological agenda.

### **Terrorist Group Involvement**

The involvement of terrorist groups and their support personnel in the illicit movement of consumables began in the 1980s. The activities of the business people in the Middle East and Asia became a model in how to succeed in making money when most normal government or civil operations in these regions had become impotent or nonexistent. Terrorist groups and terrorist support networks observed how in uncertain or extreme times business people were still making money and had adapted to the cultural changes and hardships.

This was evident in the gold souks in Beirut, Lebanon, and the ad hoc gasoline service stations established along major lines of communication by entrepreneurs. These ad hoc businesses operated out of the back of vehicles and houses, and these business people were flourishing and expanding their hastily established operations. The primary reason they were so successful was that they were providing needed and luxury items to the average consumer after the economic system in the region had basically collapsed due to conflict or natural disaster. These business people were so resourceful it has been reported they were actually tunneling under the Israeli defense lines into the Gaza Strip bringing in gold and cigarettes from Egypt.<sup>1</sup>

Selling their goods, these businessmen were evading import duties and sales and use taxes. In addition to the tax evasion, the business people were committing fraud by offering counterfeit products and providing products that had been obtained illegally for sale at cheaper prices, as well as doctoring products.

This type of system was easily adaptable to most regions of the world. It became a more important method of obtaining funds as countries began to raise the taxes levied on consumables to overcome budget deficits of the late 1980s and early 1990s. At the same time, governments in Europe and North America raised the taxes levied against tobacco products and alcohol in hopes of reducing their use. Although initially this did lower the demand for these items, it also made illicit trafficking more profitable. Entrepreneurs began to establish front companies and offshore businesses in Cyprus, Gibraltar, the Isle of Man and the Isle of Wight in the United Kingdom, and Bermuda and the Bahamas in the Caribbean. These businesses were established for the sole purpose of moving normally legal commodities (cigarettes, alcohol, and gasoline) through illicit channels to avoid the taxes and import duties associated with them.

### **Illicit Cigarette Trafficking around the World**

**In Europe:** The IRA was one of the first groups to begin using cigarettes to fund their activities. Investigations by the Gardaí (Irish National Police), the Royal Ulster Constabulary (RUC), Scotland Yard, and U.K. Customs have led to seizures of cigarettes worth millions of dollars, as well as arms and explosives associated with the cigarette trafficking schemes. The IRA involvement in the illicit cigarette trade was due to the rise in taxes on cigarettes in the United Kingdom, Ireland, and most of northern Europe. By illicitly trafficking in cigarettes, and thereby avoiding the taxes and import duties, the IRA would be able to make an enormous profit. Current estimates place the amount of money made from the trafficking of illicit cigarettes by the three primary factions of the IRA, the Provisional IRA, Real IRA, and the Continuity IRA, at more than \$100 million in just the past five years. According to police figures, the Provisional IRA is the biggest fundraiser generating \$8.3 million to \$13.2 million annually. This is compared to the Real IRA, which raises \$8.3 million

annually, as well as the Loyalist Volunteer Force, which raises \$3.3 million and the Ulster Volunteer Force (UVF), which raises \$2.5 million annually. A senior police officer in Northern Ireland stated that the Real IRA now resembles a criminal organization that sometimes carries out acts of terrorism rather than a terrorist group that has to dabble in crime.<sup>2</sup>

In keeping with a current trend in terrorist financing, dissident Irish republicans have joined forces with criminals in Britain to raise millions of dollars through cigarette trafficking and the sale of illegal fuel. According to British police information, the Real IRA has crossed the Irish Sea to Great Britain to expand their illicit operations. A report from a British House of Commons select committee stated that approximately \$30 million was raised annually by paramilitaries on both sides of the sectarian violence in Northern Ireland.

A British Minister of Parliament was reported as claiming that an Irish charity worker, employed to distribute aid in war-ravaged Croatia, was secretly setting up contacts with weapons smugglers in the Balkans.<sup>3</sup> The charity worker had been known to Garda intelligence for 10 years prior to his post with the charity Irish Aid. The Minister of Parliament went on to state that the charity worker's employment in the Balkans occurred some 10 years after Garda intelligence had identified him as the leader of the Continuity IRA. The deals established in Croatia were an exchange of funds acquired from trafficking in illicit cigarettes for arms and ammunition.

**In the Middle East:** The Kurdish Workers Party (PKK) is involved in the trafficking of contraband cigarettes and tax stamps. In one particular instance in 2000, the Turkish military and Turkish federal police conducted a raid at a PKK safe house, which was suspected of actually being one of the PKK headquarters for eastern Turkey. Initially, the Turkish authorities were expecting to find caches of arms, ammunition, and explosives. But the authorities actually found a gravure printing press for producing counterfeit tax stamps and other forged documentation.

The European Union commission on cigarette smuggling named the PKK as a "Kurdish Terror Network" regarding the group's involvement in the illicit trafficking of cigarettes.<sup>4</sup> The EU Commission report states the PKK made large sums of money marketing smuggled U.S. cigarettes into Iraq across the Turkish border. The EU also alleges that the PKK has been smuggling American brand cigarettes into Iraq, where Saddam Hussein's son Uday would then control the cigarettes. Reports indicate that Saddam Hussein made as much as \$2.7 billion annually after 1991 on the cigarette and oil smuggling business.

Other terrorist organizations that have turned to illicit cigarette trafficking to provide funding are Hezbollah, Hamas, Islamic Jihad, and al Qaeda. Law enforcement research indicates that people connected to al Qaeda are involved in moving contraband cigarettes and counterfeit tax stamps throughout the United States and Europe. Al Qaeda sleeper cells establish legitimate businesses and move the illicit product through the normal domestic market, effectively hiding their operations in plain sight.



Counterfeit Marlboro cigarettes, with affixed counterfeit California cigarette tax stamp. The cigarettes were part of shipment traveling from China to Los Angeles and were intercepted in Vancouver, Canada, by Canadian Customs.

**In the United States:** An ATF investigation initiated in 1996 with the Iredell Sheriff's Department in North Carolina illustrates the illicit cigarette trafficking in the United States. This case involved a cigarette trafficking scheme in North Carolina, a low tax state, from which millions of dollars' worth of cigarettes were smuggled to Michigan, a high tax state. The defendants, 25 in all, were moving cigarettes by rental vehicles from Charlotte to Detroit to sell on the streets. Proceeds were then transferred by wire and by courier to bank accounts in Beirut, Lebanon. Portions of the proceeds were used to provide material support to the Hezbollah international terrorist organization in Lebanon. In 2001, a federal grand jury in Charlotte indicted the 25 persons for money laundering, cigarette trafficking, conspiracy, and immigration violations. To date, 20 defendants have been

convicted for violations of the Contraband Cigarette Trafficking Act (CCTA), conspiracy, money laundering, and immigration violations. In addition, three of those

defendants were found guilty of providing material support to a terrorist organization (Hezbollah). Five defendants remain fugitives. This investigation resulted in seizures of cigarettes, real property, and currency worth close to \$2 million dollars.

In another investigation into the trafficking of contraband cigarettes prior to the traumatic events of September 11, 2001, ATF discovered that a convicted cigarette trafficker was tied directly to Hamas. During the execution of search and arrest warrants, the suspect stated, when asked about the identity of a person in his residence, that the man was his cousin and that he was in Hamas, and that he had come to the United States to escape from the Israelis.



Counterfeit Marlboro cigarettes purchased from a Web site operated out of New York State, during an ATF undercover buy.

**On the Internet:** In addition to the interstate and international trafficking of illicit cigarettes for profit, research indicates that the terrorist groups are beginning to get involved in the Internet sales of cigarettes. The Internet is a busy marketplace, and operating an Internet site doesn't require sellers to establish a business within the United States or Europe. People or groups that operate Internet-based cigarette sales can set up operations in places such as Gibraltar or the Colon Free Trade Zone and sell their contraband cigarettes in any state within the United States or any country in the world without actually having to be present in the state or country. Internet sales of cigarettes are robbing states of millions of dollars annually. Current laws are not designed specifically to regulate the Internet sales of cigarettes. The violation of the current law (known as the Jenkins Act) is a misdemeanor and is difficult to prosecute in a federal court when other criminal charges are not viable.

### Economics of Illicit Cigarette Trafficking

Just what are the economics associated with terrorist involvement in the trafficking of illicit cigarettes? First, of course, are the funds that are lost by the states and the federal government due to the trafficking. It is estimated by state and federal tax authorities that by the year 2005, the combined state losses due to illicit cigarette trafficking could reach into the billions of dollars. This is critical in today's economy, when the majority of states are experiencing record deficits and are looking to raise the taxes on cigarettes to supplement their budget shortfalls.

Second, the monetary support gained by the terrorist groups from the trafficking can cause much more than fiscal harm to the United States and its allies. With the funds received from the trafficking of illicit cigarettes, terrorist groups can purchase more arms, ammunition and explosives and use them against the United States and its interests, putting U.S. citizens at risk, as well as providing for a climate of fear around the world. Law enforcement intelligence, as well as credible open source information points to a definite benefit to terrorist groups from the illicit sale of tobacco.

To fully understand how terrorist funding is being supported by illicit cigarette trafficking it is necessary to fully understand the methodologies involved, as well as the various schemes used to traffic the illicit cigarettes. In addition, to fully combat the growing problem of illicit cigarette trafficking, law enforcement must be proactive in its investigations, including recognizing the current and future trends regarding illicit cigarette trafficking.

### Methodology

A key to the current methodology of the terrorist groups and people that provide them with material support is provided in the earlier reported statement by a senior police officer from Northern Ireland. He said the Real IRA is "looking more and more like an organized crime group that also conducts terrorist acts, rather than a terrorist group that conducts criminal acts." This statement is key because it reveals the new face of terrorism.

Terrorist groups, on the whole, have changed their face within the past decade. With the integration of world markets and the push for a more equal global trading system, terrorist groups have also shifted their focus to infiltrate the ever



Counterfeit Michigan cigarette tax stamps. This sheet is one of hundreds, each representing thousands of counterfeit tax stamps, obtained during raid conducted in the Dearborn, Michigan area.

expanding global trade and world markets. The new face of terrorism does not include the traditional organizations or enterprises of the past. The new face is totally different. It is more goal-oriented, and it has no problem integrating perfectly legal enterprises with criminal or illicit enterprises.

T. R. Young stated that organized crime is a growth industry in the United States. His view is that organized crime constitutes between 10 percent and 25 percent of the gross national product.<sup>5</sup> With these figures, it is easy to understand why terrorist groups are beginning to act and operate in

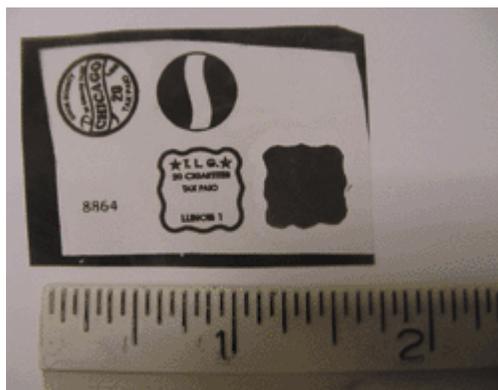
ways that are strikingly similar to organized crime. Organized crime's influence in world politics, world trade, and arms proliferation has grown tenfold since the opening up of Eastern Europe. It is no wonder many terrorist groups are working practically hand-in-hand with organized crime in order to obtain material and financial support for their organizations.

In many aspects the material support to terrorist organizations is based upon ethnic or cultural connections. With this in mind, both Europe and North America have seen a rise in immigrant involvement in criminal acts, including money laundering and fraud. Europe is having an extremely difficult time combating the amount of crime perpetrated by Albanian, Asian, and Russian organized criminal groups. The United States, although experiencing a decline in traditional organized crime groups such as the La Cosa Nostra, has seen a large rise in the amount of organized criminal groups ethnically tied to the Middle East and North Africa.

#### Establishment of Illicit Operations

How then do these "businesspersons" establish themselves in the United States? What allows them not only to succeed but also to expand their operations?

The general order of establishment is for the "family" to emigrate from their homeland singly but as part of a line of emigrants. They eventually become immigrants in Europe and North America and establish themselves and their family in retail and wholesale business ventures. In order to establish the business operations in the United States, the head of the family will usually immigrate to establish a retail sales or import-export trade business. The one uncompromising rule in the initial establishment is that it must be a male, which is the cultural norm for populations residing in southeast and southwest Asia and the Middle East. While there may be members who are not directly tied to the family, the norm is for family members to actually operate the business. In the case of the Middle Eastern criminal enterprises, the family will generally include fathers, sons, male cousins, uncles, and brothers.



Templates for printing counterfeit Chicago/Cook County and Illinois State cigarette tax stamps. The templates

#### The Schemes

There are various schemes used to traffic in illicit cigarettes. Some of the more obvious or most common schemes are trafficking from a low-tax state to a high-tax state, Internet and mail order sales, theft and hijacking, import-export operations, and counterfeiting cigarettes and tax stamps. Many of these schemes are used domestically and internationally and are often used in conjunction with other schemes. It's also not unusual for criminals to switch back and forth among schemes in an attempt to evade law enforcement scrutiny.

were recovered from a suspect who traveled from the West Bank in Israel to Amman, Jordan, and then flew to Chicago. Had the stamps been used, Chicago/Cook County and Illinois State would have been defrauded out of nearly \$5 million in uncollected tobacco tax revenue.

These are the trafficking schemes of choice among terrorist groups and the people that support them. The groups know it is important to be flexible. More than one scheme can be used depending on several

factors including market forces and law enforcement scrutiny. Under pressure or scrutiny, it is common for the groups to turn to other crime or go underground. Once they come under scrutiny for cigarette trafficking, they will change to something else, such as gasoline fraud, food stamp fraud, and psuedoephedrine trafficking.

The sources of the illicit cigarettes come from several areas. They come from low-tax states, from a foreign free trade zone, from a customs bonded warehouse, from certain Native American reservations, from stolen or hijacked shipments, and from manufacturers of counterfeit cigarettes overseas.

### Trends

Estimates from the various state tax officials show a decline of approximately \$1.4 billion in revenue collection due to illicit cigarette trafficking. This figure, which is a 2001 estimate, shows just how lucrative cigarettes have become. Many states are reporting revenue losses; in 2001 nine states' combined loss was approximately \$850 million. An IRS study has shown that, combined, states show over \$1 billion in losses to non-taxed sales of cigarettes. To compound the problem, states continue to raise cigarette taxes as an easy way to raise needed revenue.

Just as with the organized crime groups of the past, terrorist organizations are drawn to illicit cigarette trafficking due to the possibility of large profits for little work. With the variations in state taxes levied on a pack of cigarettes nationwide, the illicit trafficker can make millions of dollars a year.

Indications are that terrorist involvement in illicit cigarette trafficking will grow. Each state that raises its cigarette taxes is a new prospect for illicit profits gained by trafficking in cigarettes.

In addition, the current relationship between terrorist groups and criminal groups will continue to grow. With the amount of profits obtained through illicit cigarette trafficking both types of organizations can benefit. This problem will not simply go away. The organizations and support mechanisms are fully entrenched in illicit cigarette trafficking operations. In some instances, the trafficking of illicit cigarettes are their only known means of support.

<sup>1</sup> Stephen Farrell, "Smugglers' Tunnels Undermine the Israeli Security Cordon," The Times (London), May 20, 2002.

<sup>2</sup> "Ulster Cigarette Smuggling Shock," Belfast Telegraph (Belfast, Northern Ireland), December 21, 2000.

<sup>3</sup> Donna Carton, "Aid Worker Used Balkan UP Weapons Pipeline for Mercy Mission to Set Rebel IRA Terrorists," Sunday Mirror (London), December 17, 2000.

<sup>4</sup> "The PKK Is a Terrorist Organization," Turkish Press Summary, March 27, 2002.

<sup>5</sup> T. R. Young, Socgrad Mini-lectures, The Red Feather Institute, September 1999, <http://www.rf-institute.com/lectures/047techcrm3.htm>.

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