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THE MODUS OPERANDI OF CIGARETTE SMUGGLING IN MALAYSIA

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Financial support from
The Rockefeller Foundation and
Thai Health Promotion Foundation

THE *MODUS OPERANDI* OF CIGARETTE SMUGGLING IN MALAYSIA

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ABSTRACT

The Government of Malaysia acknowledged the dangers of cigarettes on health, through the Food Act 1983 which imposed certain policies on cigarette advertising and promotion. Giving free samples is prohibited under this law. These policies were intended to reduce smoking prevalence, but the morbidity studies conducted in 1997 showed that the prevalence had increased by 5% from 10 years earlier, when the first of such studies was conducted in 1987. There was no indication, however, of smoking among the children in the present study. The findings of the study could be flawed because our observations constantly show that cigarette smoking among younger Malaysians and young school children are on the rise. In addition to increased prevalence, there is a worrisome increase in cigarette smuggling, which makes the cigarettes available at slightly cheaper prices.

There is a clear-cut difference in the *modus operandi* of cigarette smuggling in Malaysia, between whites and kretek. The latter which are from Indonesia are smuggled by boats and landed on one of the Malaysian shores, stretching from Lumut on the west coast of Peninsular Malaysia to Kuantan on the east coast. In the East Malaysian states of Sabah and Sarawak, smuggling of Kretek has been observed at Miri and Bintulu in Sarawak and Lahad Datu, Sandakan and Tawau in Sabah. The same locations in Sabah and Sarawak are also used to land whites.

The smuggling of whites takes on a more sophisticated method, seemingly through the legal channel. Whites from Europe and the Far East are brought in containers by vessels to the Singapore Port or directly to one of the ports in Malaysia, declared not as cigarettes but as non-taxable goods. Alternatively, these cigarettes are declared as transshipment goods destined for a third country. As transshipment goods, they are not taxable and need not be examined by the Customs. On the way out to their destinations, these containers are instead smuggled into Malaysia.

According to the cigarette industry, contraband and counterfeit cigarettes accounted for 21 per cent of the market share of cigarettes sold in Malaysia, costing the Government about RM1.2 billion (US$316 million) a year in unpaid duties. The amount confiscated by the Customs annually is far less, amounting to only about RM78 to RM80 million (US$20 to $21 million).

To curb smuggling, the Customs used scanning machines to determine the content of the containers before they are being sent for exports, especially those that are being suspected to have false declaration. For locally manufactured cigarettes, security inks have been required to be printed on each pack, while imported cigarettes must carry banderol labels. Tracking teams are also now actively manning the shores of Malaysia, especially where smugglers were known to land their goods. The Customs will apply these available laws to more effectively curb smuggling, and also increase the fines for smugglers found guilty and the smokers who are caught smoking DNP cigarettes.

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TABLE OF CONTENTS

		Page
	ABSTRACT	2
	ACKNOWLEDGEMENTS	4
1.0	**BACKGROUND OF CIGARETTE SMOKING IN MALAYSIA**	7
2.0	**BACKGROUND OF CIGARETTE SMUGGLING**	13
3.0	**BACKGROUND OF CIGARETTE SMUGGLING IN MALAYSIA**	19
4.0	**DATA**	24
5.0	**SMUGGLING AREAS**	26
6.0	**MODUS OPERANDI**	28
6.1	*Modus Operandi: Contraband Cigarettes*	28
6.2	*Modus Operandi: Kretek Smuggling*	30
7.0	**ESTIMATES ON THE AMOUNT OF SMUGGLED CIGARETTES**	33
8.0	**MEASURES TO CURB CIGARETTE SMUGGLING**	38
9.0	**CONCLUSIONS**	41
	REFERENCES	42
	APPENDICES	44
	APPENDIX A: FACTS ON MALAYSIA	45
	APPENDIX B: NATIONAL HEALTH AND MOBIDITY SURVEY, 1996	52

LIST OF TABLES

		Page
Table 1:	Smoking Prevalence by Selected Demographics (1986, 1996)	8
Table 2:	Price List of Major Brands of Cigarettes as of April 2003	12
Table 3:	Quantity, Value, and Estimated Duty from Smuggled Cigarettes (1999-2003)	36
Table 4:	Quantity (kg) of Smuggled White Cigarettes as per Percentage of Sales	37
Table 5:	Prevalence of Ever Smokers by Socio-demographic Characteristics (Age >=18 years)	52
Table 6:	Prevalence of Current Smokers by Socio-demographic Characteristics (Age >=18 years)	55
Table 7:	Mean Initiation Age of Ever Smokers by Socio-demographic Characteristics (Age >=18 years)	58
Table 8:	Distribution of quit attempts among current smokers over the Previous one-year period by Socio-demographic Characteristics	60
Table 9:	Mean number of attempts to quit among those who ever tried by Socio-demographic Characteristics	62
Table 10:	Prevalence of Current and Ex Smokers among Ever Smokers by Socio-demographic Characteristics (Age>=18 Years)	64
Table 11:	Type of Smoking by Socio-demographic Characteristics	68
Table 12:	Distribution of Light, Moderate and Heavy Smokers among Current Smokers	71

LIST OF CHARTS

		Page
Chart 1:	Prevalence According to Different Income Types	9
Chart 2:	Distribution of Current Smokers by Age Groups	10
Chart 3:	The Map of Malaysia: Indication of Smuggling Areas and Directions of Smuggling into Malaysia	27

1.0 BACKGROUND OF CIGARETTE SMOKING IN MALAYSIA

The Ministry of Health, Malaysia conducted the first morbidity survey in 1986 to determine smoking prevalence and other behaviors related to cigarette smoking. But prior to that the survey, Malaysia had already introduced anti-smoking policies under Section 34 and 36 of the Food Act 1983. The policies contained several measures to restrict the availability and promotion of cigarettes to the public, among others, the prohibition of direct advertising of tobacco products in all media. Cigarette vending machines and distribution of free samples was also prohibited, although due to poor enforcement of policies, cigarette companies did not stop giving out free samples. The Trade Description Act 1972 requires that cigarette boxes carry the warning label "Smoking Endangers Health".

The second morbidity survey by the Public Health Institute, Ministry of Health published in 1999, showed that the national prevalence of current smoking was 25% or one in four adults were found to smoke at the time of the survey (see Table 1). A similar survey conducted 10 years earlier (in 1986) reported the prevalence of smoking at one in five or 20%. Over a ten-year period, the 5% increase in smoking prevalence is quite substantial. Furthermore, this increase took place while several measures were implemented by the government to reduce smoking habits among the population.

Males remained as the biggest group of smokers as compared to females. This has not changed through the years, although there was a slight drop among the number of female smokers. The prevalence across ethnic groups, however, varied quite considerably. Across the two survey periods, the Malays tended to have more smokers than the Chinese and the Indians, although more heavy smokers were found among the Chinese.

Table 1
Smoking Prevalence by Selected Demographics (1986, 1996)

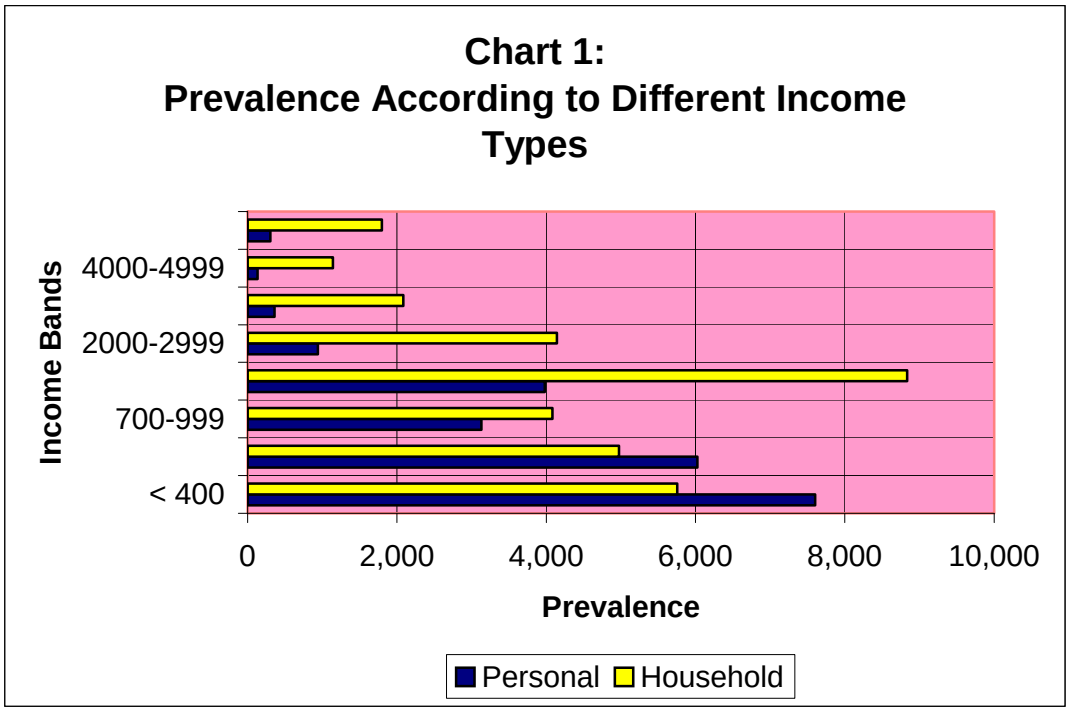
	NHMS1 (1986)	NHMS2 (1996)
Studied Population	Adults above 15 years	Adults above 18 years
Coverage	Peninsular Malaysia	Whole of Malaysia
Prevalence of Current Smokers	21.5%	24.8%
- by gender		
Males	41%	49.2%
Females	4%	3.4%
- by ethnicity		
Malays	24%	28%
Chinese	18%	19%
Indians	15%	16%
- by Location		
Rural	23%	29%
Urban	19%	22%
- by State		
States with highest prevalence	Kelantan, Trengganu, Pahang	Kelantan, Trengganu, Pahang
Age association	Increase with age	Increase with age
Income association	Higher in low-income group	Higher in low-income group
Smoking categories		
- Low: Moderate: Heavy	33% 33% 33%	31% 36% 33%
- Ethnic group association	More heavy smokers among the Chinese	More heavy smokers among the Chinese
-Household income group association	Higher household income higher proportion of heavy smokers	Higher household income higher proportion of heavy smokers
Quit ratio (Ex-smoker : Current Smoker)	1:6 (highest in Negri Sembilan and among high income and education level group)	1:5 (highest in Negri Sembilan and among high income and education level group)

Source: National Health and Morbidity Survey, 1996. Kuala Lumpur: Public Health Institute, Ministry of Health, Malaysia, 1999.

Table 1 above shows that the rural areas recorded more smokers than their urban counterparts, but both locations recorded an increase in prevalence across the two study periods. Unfortunately, prevalence was higher among the low-income group than the higher-income group, implying that poor people suffer the most from the side effects of smoking. It complements the findings that prevalence was highest in the three east-coast states of Kelantan,

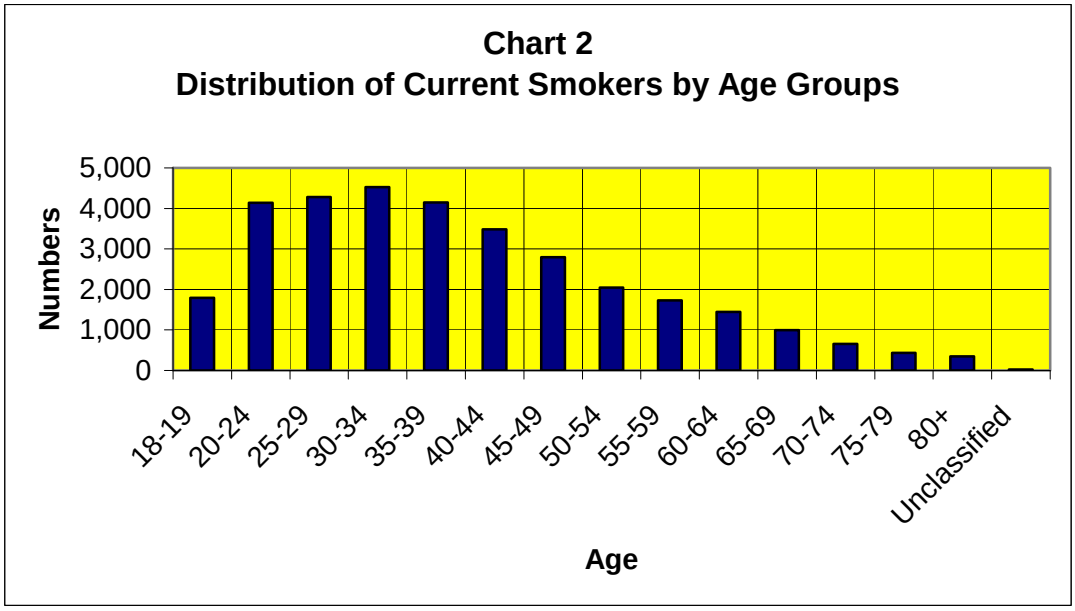
Trengganu and Pahang, which comparatively have the greatest number of poor people in Malaysia.

Smoking variations were also discovered to be closely associated with income types. Higher smoking prevalence is more closely associated with household rather than personal income. More household members who are working and smoking can contribute to disposable income and hence, an increased prevalence (see Chart 1 below). This may again explain the extent of sharing in the consumption of cigarettes, which is related to the behavior among the Malaysian smokers. This may not be true of the smokers in the Western countries, who seldom share their cigarettes.



Source: National Health and Morbidity Survey, 1996. Kuala Lumpur: Public Health Institute, Ministry of Health, Malaysia, 1999.

It was unfortunate that this study by the Public Health Institute selected samples from adults only, excluding household members below 18 years Smoking prevalence among children is on the rise, the data in Appendix B show that 8.4% of the current smokers are classified as "Schooling". Chart 2 below shows the distribution of current smokers by age groups.



Source: National Health and Morbidity Survey, 1996. Kuala Lumpur: Public Health Institute, Ministry of Health, Malaysia, 1999.

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According to this study, adults could start smoking as young as 18 years old, there is evidence of smoking among the secondary school children as early as 13 years old. Indeed, as the chart above indicates smoking is a function of age: lesser number of smokers was observed among the older groups. The prevalence started to decline beginning with the age of 40. The highest incidence of smoking was recorded among the younger groups, within the ages of 20 to 39.

We know that the youth and the poor are the most affected by price increases; the fact that they have high smoking rates suggests that they are likely to purchase smuggled cigarettes when they have access. The present study recorded that the customs are aware of the availability of smuggled cigarettes at a cheaper price through the black market (around 50 cents cheaper a pack compared to Duty-paid (DP) cigarettes) to those smokers familiar to the retailers. This means that the buyers must be "regular customers" in order to buy cheaper smuggled cigarettes. Shopkeepers are cautious to sell smuggled cigarettes because they know that it is illegal to do so. These cigarettes which are cheaper could create the false impression to the smokers that it is not a financial burden to smoke, and this would not effectively generate the concern among the younger and lower-income smokers to quit.

The regular cigarette prices according to popular brands are shown in Table 2 below. Based on the prices of cigarettes across brands, there are apparently two groups of cigarettes in the market: one group can be labeled as the premium brands, while the other the non-premium brands. The premium brands sold at RM5.40 (US$1.50) for a pack of 20 are Marlboro, Dunhill, Benson & Hedges, Salem, Mild Seven, Peter Stuyvesant, Kent, Lucky Strikes and Camel. The American cigarettes, particularly Marlboro, Salem, Lucky Strikes and Camel are popular among the younger smokers but who are indeed among the up-market smokers. The indirect advertisements of these cigarettes are clearly targeting to these smoker groups. The lesser premium brands sold at RM4 (US$1.05) for a pack of 20 are L & M, Pall Mall, Winston, Perillys, More and Goldleaf and they are popular among the lower-end of the market.

Kretek is an entirely different group of cigarettes. The three brands of Kretek available in the Malaysian market are Gudang Garam, Sampoerna and D'jarum. Gudang Garam is priced at RM3.50 (US$0.92) for a pack of 16, while Sampoerna and D'jarum at RM4.50 (US$1.18) for a pack of 20. Gudang Garam is sold in a pack of 16, which is slightly different from Sampoerna and D'jarum.

Besides Kretek, premium cigarettes are also available in small packs of 10 and 14 sticks sold at seemingly "cheaper" prices. These cigarette packs which are priced around RM4 per pack (US$1.05), could appeal to low income groups and youth, who might not afford the bigger packs of 20, normally priced slightly higher at RM5 to RM6 per pack (US$1.30 to 1.50). Observations in the past indicated that youth prefer these pack sizes, or they tended to start on smaller packs and migrated to bigger ones later once they could afford it.

Table 2
Price List of Major Brands of Cigarettes as of April 2003

Brands	Price According to Pack Size (RM)			
	20's		14's	10's
WHITES	**Premium**	**Non-premium**		
Marlboro	5.40	-	3.90	3.00
Dunhill	5.40	-	3.90	3.00
Benson & Hedges	5.40	-	3.90	3.00
Salem	5.40	-	3.90	3.00
Mild Seven	5.40	-	-	-
Peter Stuyvesant	5.40	-	3.90	-
Kent	5.40	-	3.90	-
Lucky Strike	5.40	-	3.90	-
Camel	5.40	-	3.90	-
L & M	-	4.00	-	2.20
Pall Mall	-	4.00	-	2.20
Winston	-	4.00	-	2.20
Perillys	-	4.00	4.30 (25's)	-
More	-	4.00	-	2.20
Goldleaf	-	4.00	-	2.20
KRETEK	20's		14's	10"s
Gudang Garam	3.50 (16's)		2.80 (12's)	-
Sampoerna	4.50		3.40	1.70 (7"s)
D'jarum	4.50		3.40	-

Note: RM3.8 = US$1
Source: Different price lists published by the cigarette manufacturers.

2.0 BACKGROUND OF CIGARETTE SMUGGLING

Although there were several articles on cigarette smuggling in Asia, most of the literature has been written on smuggling in Europe and North America. Smuggling is indeed an issue that has to be handled strategically, as evidenced from what has happened in Canada and some European countries.[1]

Central Issue

The central issue of cigarette smuggling is quite clear. Because taxes are illegally evaded on smuggled cigarettes, the government tends to lose in terms of revenue. In addition, duty unpaid smuggled cigarettes would be available rather cheaply. Cheaper cigarettes induce consumption, especially among the poor and youth who could smoke more, now that cheaper cigarettes are available to them. Consequently, it has become a critical public health problem, when increasing consumption of cigarettes has led to increasing burden of smoking-related diseases such as heart and lung diseases, hypertension and the like. Above all, however, smuggling is against the law and therefore, it is a crime that has to be abolished.

Characteristics of Cigarette Smuggling

Cigarette smuggling is a large-scale lucrative activity involving "illegal transportation, distribution, and sale of large consignments of cigarettes and other tobacco products, generally avoiding all taxes. This type of smuggling usually involves millions of cigarettes that are smuggled over long distances, often involving large organized crime networks and sophisticated systems for distributing smuggled cigarettes at the local level".[2]

Although, cross-border shopping could increase cigarette sales in countries where prices are cheaper, the volume is rather small because purchases of the so-called duty-free cigarettes have been merely for personal consumption. It is the organized smuggling and to a certain degree bootlegging,[3] are the biggest

[1] Luk Joossens and Martin Raw *Cigarette Smuggling in Europe: Who really benefits?*, BMJ, 1995 (May), Vol. 310, 1393-1397.

[2] "Issues in the Smuggling of Tobacco Products" in *Tobacco Control in Developing Countries*. eds. Prabhat Jha and Frank Chaloupka. Oxford, New York: Oxford University Press, 2000.

[3] bootlegging is legally buying cigarettes in a low-tax country and illegally selling them in a high-tax country.

concerns, because these two activities involve movement of large volume of cigarettes from countries which have cheaper cigarettes to countries with higher-priced cigarettes. It is the organized cigarette smuggling that poses varied problems to the governments of countries where smuggling is directed at.

However, the party to be blamed is the authority including the customs and other enforcement agencies who fail to enforce sufficient control. When the control is inadequate coupled with corruption of staff of enforcement agencies, smuggled cigarettes could easily make their way to the market. The cigarettes which are purportedly to be exported are leaked out into the local distribution networks. Therefore, "up to one-third of recorded cigarette exports do not reappear as recorded imports"[4]

Jha and Chaloupka also noted that organized smuggling worldwide has the following characteristics:[5]

- involve international brands:

  as was discovered in Europe and North America, only international brands were smuggled, especially if the cigarettes were cheaper in the country of origin;

- in-transit system

  smuggling occurred while in transit. Cigarettes were declared as exports destined for a third country. Such goods were not taxable at the transit ports;

- a wide range of owners

  many parties including middlemen were normally engaged in smuggling. All of them made up a supply network;

- organized criminal networks plus corruption

[4] "Issues in the Smuggling of Tobacco Products" in *Tobacco Control in Developing Countries*. eds. Prabhat Jha and Frank Chaloupka. Oxford, New York: Oxford University Press, 2000.
[5] Ibid.

smuggling syndicates were organized criminal networks whose success depended a great deal on the cooperation of corrupted local officials;

- good local distribution networks, plus street-selling.

  Smuggling syndicates do not normally have networks to distribute the cigarettes, therefore, they had to rely on local distributors which were street sellers themselves. In Malaysia these could include retail shops and restaurants. Smuggled or regular cigarettes are sold in the same store, but smuggled ones are sold secretly only to buyers whom retailers know. According to the customs officials, smuggled cigarettes are sold cheaper than non-smuggled ones.

Modus Operandi

Smugglers took a lot of trouble to smuggle cigarettes, primarily because it is a lucrative business especially when relevant taxes were not paid. For the European markets, cigarettes were shipped in containers from the United States, directly to selected northern European ports of Antwerp, Rotterdam and Hamburg. The cigarettes were declared as goods-in-transit destined for Northern African states. Because the goods would be shipped out to another country, no tax was required to be paid. Joossens and Raw[6] noted that the essence of transit system is to facilitate trade by allowing the temporary suspension of customs duties while under transport across a defined customs area.

To prove that cigarettes were for export, the smugglers or their agents presented completed transit documents showing that the cigarettes have arrived in importing countries. With or without the help of relevant officials, the documents were forged to show that the cigarettes had arrived in the intended countries although they had not. At this point, the cigarettes were switched from one lorry to another to escape detection, until they had been successfully distributed into the networks in the country.

Alternatively, the cigarettes were actually being exported to the destined countries outside the European Union, subsequently smuggled back into the country, often by speedboat through selected transit points notably Andorra,

[6] http://bmj.bmjjournals.com/cgi/content/full/310/6991/1393?maxtoshow=&HITS=10&hits...

Gibraltar and several other towns. Poor authority checks at these points had facilitated movement of the smuggled cigarettes into intended destinations. The passages through Andorra and Gibraltar were considered the traditional routes to smuggle the cigarettes into the European Union countries. The modus operandi varied quite considerably.

The modus operandi to smuggle cigarettes into Eastern Europe and the former Soviet Union was by road trucking. Cigarettes were first transported from Belgium to Switzerland. Being outside the EU law, it was easy for the cigarettes to be trucked out of Switzerland into the intended countries.

Smuggling was also conducted by air. Starting from the ports where cigarettes were stored in warehouses, the cigarettes were transported to regional airports in Belgium or the Netherlands, and then flown to Eastern Europe in containers. From Eastern Europe they were rerouted into the European Union countries by road or water using speed boats.

Ports in Northern Europe were also used as the starting points. To avoid paying taxes, the cigarettes were declared as transit items destined for northern African countries. They were then transported by sea along the Spanish territorial waters, and at an opportune time, the cigarettes were then smuggled into Spain.[7]

Joossens[8] also indicated that smuggling of cigarettes into Vietnam took the in-transit route. Cigarettes were produced in the UK then shipped to Singapore as duty free items. They were then sold to importers and traders in Cambodia, who would then transport them illegally to Vietnam.

Whatever was the modus operandi, the operation was very complex. It was deliberate, nevertheless, in order to confuse the authority and to make investigations difficult. A consignment was made more complicated when it passed through several owners and the link between them was rather unclear. Again, this was purposely done to prevent the authority from identifying the syndicate directly responsible for the smuggling.

[7] http://bmj.bmjjournals.com/cgi/content/full/310/6991/1393?maxtoshow=&HITS=10&hits...

[8] Luk Loossens, "Vietnam: Smuggling adds Value" Tobacco Control, 2003, vol.12, 119-120.

Measures to Curb Smuggling

As it has been shown in the literature, the usual argument by the tobacco industry that high taxes induce smuggling is not entirely true. Such argument has an ulterior motive to lower the tax that would consequently lower the price of cigarettes, followed by a chain of effects on unintended smoking behavior. From a broader perspective, even not taking into consideration the ill effects of smoking, smuggling ought to be curbed because it is essentially a criminal activity.

Because cigarette smuggling is a criminal activity similar to the smuggling of dangerous drugs and firearms, and involving illegal activities worldwide, any measure aiming to curb smuggling should similarly be done worldwide. Any port of entry of any country of the world today is concerned with drug and firearm smuggling, and subsequently undertakes serious control measures and strict checking of people and goods entering the country. Similarly, any country should understand the dangers of smuggling and the effects of cigarettes on health, and consequently, should enforce strict control and measures to curb if not entirely to abolish smuggling of cigarettes and tobacco-related products.

The literature outlines several measures to reduce smuggling or at least control it. As smuggling is a serious crime, the punishment on the activity has to counterbalance it. Currently, if caught the punishment on smuggling is extremely non-deterrent and therefore, fails to discourage the smugglers. The penalties were so small that smugglers were more than willing to pay them so that they can get off the hook quickly and continue with their smuggling activities. Smuggling brings them three or more times the penalties in compensation. To be more effective, many believe that penalties should "render tobacco smuggling financially unappealing." [9] In addition, the cigarette manufacturers themselves should be made responsible for the cigarettes smuggled into the country.

At the moment, cigarette packs in some countries do not have marks to indicate if relevant taxes have been paid. The governments should make it compulsory for all cigarette packs to be identified with stamps to show that all taxes have

[9] Luk Joossens and Martin Raw *Cigarette Smuggling in Europe: Who really benefits?* BMJ, 1995 (May), Vol. 310, 1393-1397.

been paid. This system would easily identify smuggled cigarettes, especially when the packs do not carry such stamps.

Along with this, the laws on tobacco taxation should require cigarette companies to have a proper accounting system of the movement of their cigarettes that have legally been transporting to intermediaries right down to the end of the distribution channel. Cigarettes that cannot be accounted for in the system are essentially smuggled ones, and therefore, companies must be held responsible, because they are the ones that produce them in the first place.

In some countries almost anyone can sell cigarettes even without a proper license. This has to be checked and probably the whole licensing structure and law be revised to ensure that only those who qualify would be able to sell cigarettes. Again, such licenses must be restricted to control the numbers of distributors and sellers, similar to the distribution of pharmaceutical products where only those licensed druggists are permitted to sell controlled drugs. In addition, since cigarette trade involves imports and exports, the end sellers should also have proper end-user certificates, proofs of purchase and relevant tax payments. These documents should be able to be traced back to the manufacturers who supply the cigarettes.

Above all, since cigarette smuggling is conducted at an international scale involving organized crime, its distribution and trade must similarly be controlled at an international level. There ought to be an international convention that would monitor and control the distribution of cigarettes internationally, coupled with the cooperation and support of all the governments throughout the world. This is envisaged similar to what has been developed to prevent smuggling dangerous drugs.

3.0 BACKGROUND OF CIGARETTE SMUGGLING IN MALAYSIA

It has been estimated that "from a world export total of 846 billion in 2000, some 227 billion cigarettes did not reappear as imports. Total loss of revenue by governments due to cigarette smuggling around the world is estimated at US$25-30 billion annually".[10] According to the World Bank, smuggled cigarettes account for one-third of all international cigarette exports, and out this amount, 355 billion cigarettes is destined for the South-East Asian market where smuggling has become a problem of immense proportion.[11]

According to customs, the above value is only the tip of the iceberg. The actual amount and value of smuggled cigarettes could be bigger. This indicates the extent of the loss of revenue to the government. Such loss implies that smuggling of cigarettes is important and represents a significant share compared to other smuggled goods such as liquor and taxable electrical goods. Cigarette smuggling should at least be controlled. To the smugglers however, the activity is highly profitable, such that they will take the risk of being caught and fined for evading the tax than to stop smuggling.

The Customs estimated that every successful smuggling attempt would result in about Ringgit Malaysia (RM) 5 million (US$1.3 million) gross incomes to the smuggling syndicate. (See detailed discussion on the amount of smuggled cigarettes in section 7.0 below.) The haul is by boats known among the customs circle as "pancung" which can load up to five Toyota Hilux trucks of cigarettes, where each truck can carry Ringgit Malaysia 1 million (US$263,157) worth of Kretek cigarettes. After deducting expenses and other payments, one successful smuggling could net about 50% of revenue or about RM2.5 million (US$657,894), which is considered to be quite a lucrative sum of money. According to the customs, that kind of money has motivated cigarette smuggling to persist such that the government will have to double the money and effort to curb it.

The Royal Customs Department of Malaysia (KDRM) announced several measures to counter cigarette smuggling and the sale of cigarettes with false

[10] The FCTC and Tobacco Smuggling: NGO Briefing for the International Conference on Illicit Trade in Tobacco, New York: 30 July-1 August 2002, page 2.

[11] Report from www.who.int/tobacco/en/atlas20.pdf

labeling. The then Director-General of Customs, Tan Sri Abdul Halil Abdul Mutalib, indicated that his department had allocated RM60 million (US$15.7 million) to increase the number of speedboats to conduct anti-smuggling patrols[12], around the Malaysian western shores in Peninsular Malaysia, where most smuggling of Indonesian kretek cigarettes took place.

Smuggling involves the diversion of large shipments of cigarettes into the black market. Once they enter the black market, it is suspected that the cigarettes will be sold at reduced prices. It could not be verified in the case of Malaysia because the smuggled cigarettes are difficult to trace to the retail outlets. The distribution was done so efficiently that the authority can only guess on when and how the cigarettes went into the distribution outlets once they were smuggled into the country.

The wholesalers could be licensed cigarette importers who have connections with overseas manufacturers, especially for kretek where, Customs found that the cigarettes in their stores had the words "*Diimport oleh …*" (or "Imported by…) printed on the packets at source, indicating that they are legally imported cigarettes. This is supposedly different if the cigarettes are smuggled, where the packets would be stamped with words in the Indonesian language labeled as "Amaran Pemerintah…" as opposed to "Amaran oleh Kerajaan Malaysia…" [13]

To differentiate between smuggled cigarettes and cigarettes whose duties have been paid (DP) is difficult. The authority has resorted to use banderol for imported DP cigarettes and security inks for locally manufactured ones whose tax has been paid. As part of the requirements of the law, local cigarette manufacturers need to have the security inks on each pack manufactured, and this supervised by the Customs on site. If these cigarettes are intended for the local market, the relevant duties have to be paid before they leave the factory. Cigarettes manufactured locally to be exported are waived on duties. For imported cigarettes, the original manufacturers need to buy the banderol from the Malaysian Customs and have it affixed to each packet before exporting. Any packet of cigarette in Malaysia without the banderol or security inks is considered as smuggled cigarettes.

Before the implementation of the security marks, the best the customs could do within the existing law was to examine the retail outlets suspected of selling

[12] Internet UICC Globalink, www.news.globalink.org/171283.shtml

[13] Both mean "Warnings by the Government of ……." but Indonesia will always use the word "Pemerintah" while Malaysia will use "Kerajaan" for the word "Government"

contraband cigarettes. In one of those past examinations, when stocks of cigarettes were not substantiated with proper documents, such as relevant invoices, they were classified as tax unpaid and subsequently confiscated. However, it would be almost impossible to carry out the stock checks, especially if they are to be done regularly. As it is, customs normally carry out the stock checks after receiving information from their informers or when they have good reasons to suspect illegal activity.

Whatever the case may be, when there is smuggling the syndicates are the one who gain the most. A Syndicate is essentially the smuggler, who is a "taukey" (a Chinese word meaning "businessman"). Working independently out of the territories of other syndicates, he is believed to have other legal businesses too. This, however, cannot be fully disclosed and proven, although the authority has the profile of the syndicate "taukey." The syndicate is not only involved in cigarette smuggling, but smuggling of other items including liquor also.

On the other hand, the loss is always incurred by the government by way of tax evasion, which could be in the millions of Malaysian Ringgit. Smuggling may favor the cigarette companies because it made available cheaper smuggled cigarettes in the black market and subsequently promotes higher demand or create new ones. In addition, with increasing smuggling activities, cigarette companies have a good reason to press for the government to lower tobacco tax that could consequently lead to increased demand.

One wonders why the syndicates could not be arrested. According to the Customs, arresting the syndicate is not that easy because it involves the law, which requires sufficient evidence or that the culprit be caught red-handed for arrest. There were times when the suspects had been brought to court, but they were discharged on ground of insufficient evidence. In addition, it is not the "taukey" himself who undertakes the smuggling but his men, popularly known as "runners" among the authority. The runners are normally paid well, around RM200 per job done, to inform the whereabouts of customs or what they plan to do.

Cigarette companies seemingly are against smuggling because they pay the relevant taxes and duties, while smugglers do not, yet they benefit from being sold in the black market. To the customs, and even to some government officers, it will not apparent to them that the cigarette companies could be involved in smuggling. Strongly believing that the cigarette companies pay the relevant taxes and duties, they are seen as positively contributing to the nation's

income and fighting hard against smuggling. Therefore, the authority would not have reasons or motivation to implicate the cigarette companies in orchestrating smuggling activities.

The delay on the part of the government to institute anti-smoking campaign (campaigns against the dangers of smoking were not launched through advertisements until March 2004) and control measures to reduce smoking was suspected to be due to the belief that cigarette revenues constitute quite a big portion of the nation's income. Undoubtedly, revenues from sales tax and duties on cigarettes and tobacco leaves are quite substantial, but the impact of smoking on health could be more expensive. If studies on the dangers of smoking can empirically show that the costs of health care on tobacco-related diseases outweigh the income from taxes and duties on cigarettes and tobacco, more governmental activities against smoking may be undertaken, including measures to curb smuggling. This can be somewhat accomplished if the *Modus Operandi* of cigarette smuggling activities is studied and understood. Then the relevant authority can effectively design measures to curb such activities and ultimately reduce smuggling substantially.

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According to a local rating agency, increased duties on cigarettes and tobacco-related products would not affect the revenue of cigarette companies in Malaysia, even if such taxes will result in price rise. "The AAA rating of British American Tobacco (Malaysia) Bhd (KLSE: BATO) [BAT] remains unaffected by the increase in the sales tax on tobacco products from 15 per cent previously to 25 per cent in the wake of the 2001 Budget announcements. Rating Agency Malaysia Bhd (RAM) reported that the broad rise in cigarette prices resulting from the Budget proposals was expected to be sufficiently high to cover the adjusted production costs and, and at the same time, allow BAT to at least maintain its overall profit margins for the financial year to December 31, 2001.[14]

An on-going problem faced by the Customs in combating cigarette smuggling however, is the extent of availability of prior information on smuggling activities. As one customs officer put it "Smugglers know what customs are doing and intend to do, but customs do not know what smugglers are doing and intend to do." The customs can only move after receiving information from their informants, which sometimes was untrue or out-dated. But, for some reasons, the smugglers tended to have better informants than the customs have.

[14] "Cigarette price rise not to affect BAT Malaysia ratings" Asia Pulse (Nov 8, 2000) or [web page] http://tobacconews.org/?StoryID=53168.

This ended with the customs in fruitless chases, having to arrive at the scene, purportedly to arrest smugglers red-handed, but to their dismay there was no smuggling. The smugglers were given the warning much earlier before the customs even left for the raid.

While the industry claimed that counterfeiting factories have been discovered in Malaysia, the matter has not been verified. If this is true, the amount of non-duty paid (DNP) cigarettes in the market is bound to escalate. The industry argues that "The government will lose out on tax revenue should demand for duty-paid cigarettes fall or if some consumers, in these tough economic times, decide to switch to cheaper smuggled cigarettes"[15] This assumes that smuggled or contraband cigarettes are cheaper than duty-paid cigarettes. Customs sources have indicated that it is true and it would be possible to buy "smuggled cigarettes" in the market as they are available to regular buyers at lower prices.

The industry also argued that the higher priced duty-paid (DP) cigarettes will, to some extent, encourage more smuggling of duty-not-paid (DNP) cigarettes into Malaysia. This is again assuming that DNP cigarettes are selling at much lower prices than duty-paid (DP) cigarettes. Customs sources believe that smuggled cigarettes are sold at much lower prices as DP cigarettes. Customs also believed that retailers had to sell smuggled cigarettes at lower prices to clear the stock quickly, so as not to be caught and fined for illegally stocking and selling such cigarettes.

[15] The Star, Monday, August 17, 1998.

4.0 DATA

The objective of this study is to determine and outline the *Modus Operandi* of cigarette smuggling in Malaysia. It is essentially a qualitative study, attempting to determine and understand how cigarettes are being smuggled into Malaysia. Where possible, the study attempted to estimate the amount of smuggled cigarettes from the interviews and from available published records.

Data were collected through one-to-one and face-to-face interviews with target respondents, principally the customs officers from the Prevention Department who had been directly involved in the prevention of smuggling and false declaration on imported goods. The present report is based on interviews with a customs head in Malacca, the head of anti-smuggling unit at the Customs Headquarters in Kuala Lumpur and another customs officer in the same office, who was formerly involved in anti-smuggling. Several other customs officers were interviewed later to get added perspectives on the issue, and because some of the officers interviewed earlier were replaced by new officers.

An official letter was first sent to the Chief Secretary of Customs, explaining the purpose of research and indicated that it was part of a study in collaboration with the Ministry of Health, Malaysia. Upon approval from the Chief Secretary of Customs, an appointment was made with the relevant individuals in-charged of anti-smuggling. Owing to the confidential nature of this study, the interviews were conducted personally by the researchers. Each effective interview lasted between 1 to 2.5 hours. In addition to the researchers, research officers were required to collect secondary data in the form of published information from the media (particularly the newspapers and the internet) and relevant government departments.

Except for recorded (written) notes, no other record of the interviews was made. This is to prevent from confidential information being abused or passed on to unauthorized persons. This procedure was observed strictly as a matter of protection to the respondents. Data was also obtained from published sources including newspapers, magazines and relevant websites.

Interviews with police and border patrol personnel, who were involved in anti-smuggling, were not carried out on the advice of customs. These departments simply supported the customs in anti-smuggling activities, and apparently have no record on the smuggling of any particular product such as cigarettes.

The study also attempted to set up an interview with an ex-smuggler to gain in-depth understandings of the motive and *modus operandi* of cigarette smuggling. However, this was not undertaken because he declined the interview at the last minute for fear of being identified as being involved in an activity deemed illegal in the eyes of the law.

The researchers were also advised against witnessing an anti-smuggling raid conducted by the police and the customs, because it would not be safe to do so and no raid was conducted within the period of the study. But the most important reason for customs seemingly not allowing the researchers to witness the raid was the newspaper report on smuggling, which indirectly implied that customs did not conduct sufficient raids to undermine smuggling and protect the government from the loss of revenue.

This report contains the findings, based on 8 in-depth one-to-one interviews, all with customs; 6 in Kuala Lumpur and one each in Malacca and Johor. We were advised not to interview officers in other regions, firstly it would duplicate findings, but more importantly the information was mostly available at the headquarters in Putrajaya.[16] The interview in Malacca was conducted before the ones in Kuala Lumpur. Malacca is the state in the south of Peninsular Malaysia. Each state has a customs department headed by a senior customs officer. Similarly, the interview in Johor[17] was conducted prior to the ones in Kuala Lumpur.

The ability to secure appointments for the interviews was very much dependent on contacts with the relevant people. Approval was difficult and it took months before the head of sections would agree to be interviewed. It would be almost impossible to secure the interviews simply through walk-ins. The fact that this study was conducted in collaboration with the Ministry of Health, helped to secure the appointments, although it took a few months before the actual interviews could take place.

Our biggest problem was waiting to interview the relevant customs officers although they never rejected the requests for interviews. Respondents were full-time employees and were occupied, but the wait was worth it, since they had all the information needed.

[16] Putrajaya is the new government administrative centre located to the south of the capital of Kuala Lumpur.
[17] Johor is the southern most state in Peninsula Malaysia. It is an important state in customs activity because of its location by being the gateway to Malaysia from Singapore.

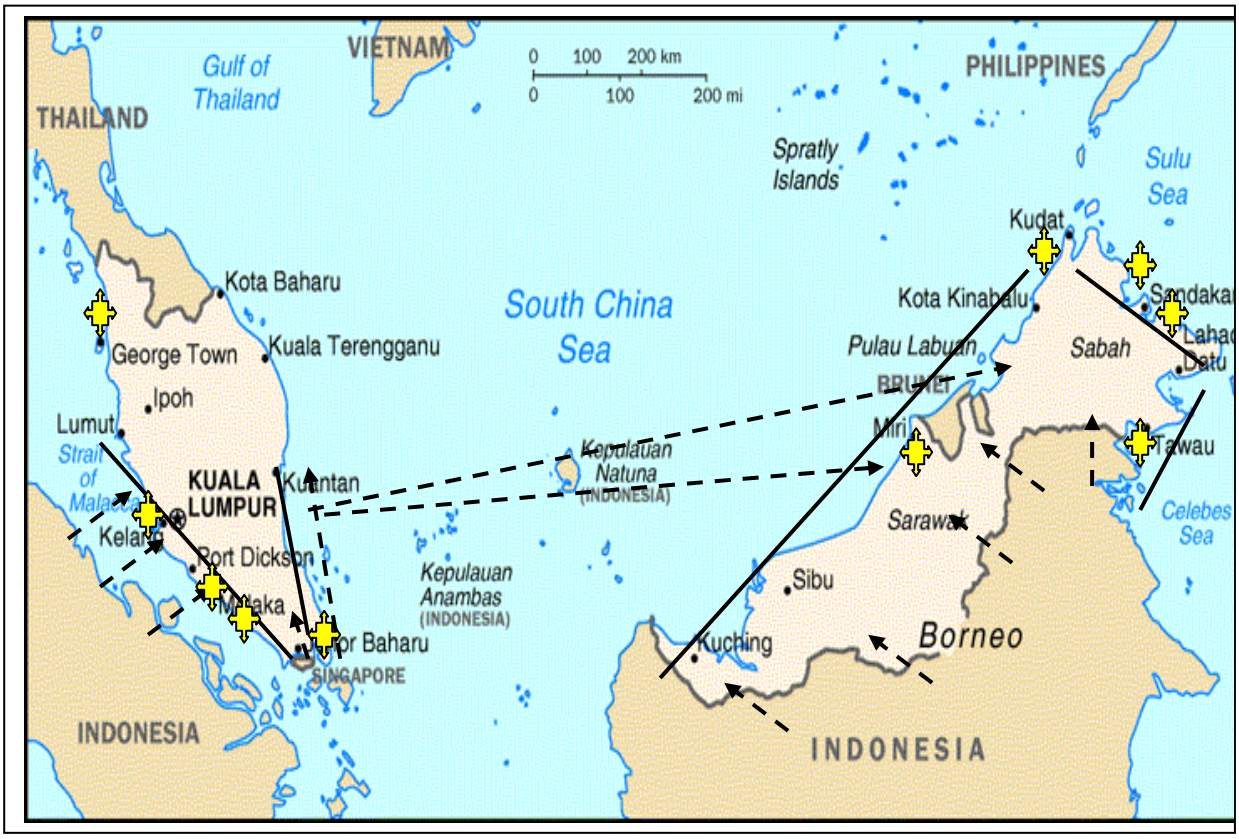
5.0 SMUGGLING AREAS

Smuggling could happen anywhere in Malaysia, and whenever the smugglers could do it. The most prominent areas were along the west coast of Peninsular Malaysia, stretching all the way from Lumut in Perak to Kuantan on the east coast of the Peninsular (see map below). The long Malaysian shores in between these two points make it difficult to curb smuggling. It would take a lot of effort, time and money to try to identify where the next smuggling would occur.

Sabah and Sarawak were also implicated as states where smuggling activities were prominent. This could be included in future studies on smuggling in Malaysia. The ports of Miri and Bintulu in Sarawak are often cited as the locations where smuggling has been observed to take place, and similarly Lahad Datu, Sandakan and Tawau in Sabah.

Smuggling along the Malaysia-Thailand border is also rampant but not for cigarettes. At this point, it is suspected that cigarette smuggling to Thailand is not beneficial because the price of cigarettes in Malaysia is much higher than that in Thailand. The two suspected areas are Perlis-Kedah and Kelantan-Thai borders.

Chart 3
The Map of Malaysia: Indication of Smuggling Areas and Directions of Smuggling into Malaysia



KEYS

Major Landing Towns

Smuggling Landing Areas

Direction of Smuggling into Malaysia

6.0 MODUS OPERANDI

A clear cut *Modus Operandi* was observed in cigarette smuggling in Malaysia. Kretek, which are exclusively from Indonesia are smuggled by boats and landed on one of the Malaysian shores indicated above.

Whites, on the other hand, are smuggled seemingly through legal import or transshipment procedures, using falsified declarations on import documents. These cigarettes are smuggled through the main ports of entry, mostly Port Klang and Johor Port in West Malaysia. Whites have been indicated to come from China, Europe (England), Hong Kong and Taiwan.

6.1 *Modus Operandi: Contraband Cigarettes*

The customs recognizes that there are two types of cigarettes being smuggled into Malaysia namely whites and kretek. Whites are essentially contraband cigarettes, being brought in quite differently from the way kretek are being smuggled.

Mostly from China but some were suspected to originate in Europe (particularly England) Hong Kong and Taiwan, the contraband whites were first exported to Singapore as goods in transit bound for a third country. The cigarettes can also be shipped directly to one of the ports in Malaysia but declared as transshipment goods that are intended for a third country.

The role of Singapore is mainly as a transshipment port. Since these goods were bound for a third country such as Malaysia, they will be stored as bonded goods at the Singapore port. To the Port of Singapore Authority, the goods in transit need not be examined, because they are not going into the country and therefore, no tax needs to be paid.

The cigarettes might be kept in the warehouse at the port for only a short time to not incur many storage charges. They were then unloaded onto feeder vessels bound for Malaysia. Often, the cigarettes could be loaded on the feeder vessels directly from the mother ship without being stored at the Singapore Port. Upon reaching Malaysia, these goods were declared as non-taxable goods, which sometimes passed on without customs examination since they were intended for export to the third countries.

Another way adopted by smugglers was to declare part of the consignment, such as two containers out of ten, as cigarettes and paid duties accordingly, while the rest or the remaining eight containers were declared as non-taxable goods. The remaining containers were cleverly stacked with the declared non-taxable goods at the front-end, while smuggled cigarettes behind the goods, making it difficult for customs to effectively examine them, unless they were prepared to spend a lot of time doing it. This was how the cigarettes escaped from paying tax.

There were cases when the containers with cigarettes were not declared at all, but reported to contain items that were non-taxable such as iron bars. Of course, the question remained why customs did not examine these containers. Actually, they did examine them, but for a given period there were thousands and thousands of containers declared non-taxable. Even if the customs were to examine all containers that were declared as non-taxable, it would take weeks before they were done. This would unnecessarily delay some genuine manufacturers from getting their non-taxable imported raw materials, mostly on Just-in-time basis for their production. In this circumstance, there bound to be a lot of complaints from the manufacturers, who genuinely need their imported raw materials for their production.

The ones that passed undetected could be the cigarettes that would finally make their way to the open market, mostly from Port Klang but also from other ports such as Penang Port on the West Coast and Johor Port in the south. The containers were unloaded directly onto container trucks and then off to be distributed to the middlemen before reaching the retailers.

In cases where the cigarettes were brought in directly through Malaysian ports, they were similarly declared as goods in transit, bound for a third country. Similarly, transit goods were temporarily stored in bonded warehouses located within the free trade zone areas. Since these goods were not taxable, they were not required to be examined by the customs, unless if they suspected otherwise.

Since these goods were in transit, they then had to be loaded onto a vessel and "exported." They were indeed loaded onto a vessel and actually left the port (country) seemingly bound for a third country. However, somewhere at sea, the cigarettes were quickly unloaded to smaller vessels, and subsequently transported back (smuggled) into Malaysia without duties being paid. Alternatively, the were brought to the private jetties and subsequently loaded onto smaller boats or right onto the waiting trucks, to be transported

unsuspectingly to the hideouts or warehouses to be kept temporarily until such time when they are safe for distribution. Sometimes, one wonders why the smugglers went on elaborate ways to smuggle the cigarettes, while there are easier ways of doing it. One reason is that the smugglers wanted to confuse the authority.

From the tone of it, cigarette smuggling was quite successful in Malaysia. Countless raids by the customs were unsuccessful, as if the smugglers knew when the raids were to be carried out. It was suspected that informers were very much involved to warn the smugglers of the raid by the authority. The informers were called "Tonto", named after the hand-man to the famous cowboy legend Lone Ranger. His job is to get first-hand information from inside sources, so that he can inform the smuggling syndicate of a possible raid by the customs.

The "business" arrangement of cigarette smuggling is the "Ali Baba" type – a partnership between a Bumiputera[18] (who is called Ali) and a Chinese (who is named Baba).[19] Each partner played a definite role, with the Bumiputera as the one who had to deal with the authority if smugglers were caught. For his share in the business, usually 10%, he had to arrange for the release of the impounded cigarettes and also the smugglers, by paying appropriate tax and fines.

The middlemen seemed to know the right persons to obtain the release, and they normally were happy to do it bearing in mind that they got their share of the 10% regardless. At this point, there was no evidence indicating the middlemen, but they were suspected of being "inside" people who worked for the smugglers. The weaknesses of the law make it easy for smugglers to evade punishment even if caught, suggesting that the law could be strengthened

6.2 *Modus Operandi: Kretek Smuggling*

Indonesia is the only source of "kretek", the famous clove cigarette. A few of the Malaysians especially the Malays have acquired the taste for Kretek, but the Indonesian immigrants remain as the main smokers of this type of cigarette. Most Chinese and Indians in Malaysia have not acquired the taste for Kretek as yet.

[18] Bumiputera literally translates as "people of the land" to refer to the Malays who were originally born in the country as opposed to the Chinese and Indians brought in as immigrants from China and India, respectively.

[19] Baba is the name given to the group of early Chinese who settled in Malacca, one of the states in Malaysia.

The *modus operandi* of kretek smuggling was somewhat different. Interesting as it seemed, the job was extremely dangerous. Smuggling was usually done by a syndicate well-armed to face any consequences. Therefore, whenever customs conducted a raid, it was always done with the police. In the future, those customs officers who will be in the anti-smuggling unit may also be armed.

Smuggled Kretek came directly from Indonesia, particularly from a town named Kediri in Java. This was where the cigarettes were manufactured. From there, they were brought to an island called Pulau Rupat, in Sumatra for storage. Pulau Rupat is located closest to Malaysia, with only 3 hours by boat to Malacca, being the nearest point from Indonesia.

Kretek were normally smuggled by boat landing directly on the nearest shores in Malaysia. As the distance is short, it is easier to smuggle directly instead of going through as whites do: brought to the ports like Singapore, declared as shipment goods or subject to false declaration and carry the risk of being detected by the authority. There is also the urgency of landing the cigarettes as quickly as possible, especially when an opportune time exists for the smugglers to do so. It is believed that the cigarettes are first brought on the boats to the islands in Indonesia, kept for hours or even days until they have been told to move to a specific location by their informants in Malaysia.

The boats normally used for direct smuggling were fast because they were powered by 55 hp engines. These boats normally landed around 3.00 in the morning. The cigarettes were unloaded onto waiting Toyota HiAce trucks (lorries). Normally these were 3-ton trucks, up to five of them would be loaded with the smuggled goods. Loading onto each truck is done extremely fast, within 30 minutes or less. This was so despite cigarettes were packed in boxes of varying sizes, implying that loaders were professionals, who knew their job extremely well. It would require more time to load if it was done by unprofessional loaders. Some of these loaders were local villagers who were fishermen or laborers earning extra money when not at sea or at work.

Once they were loaded onto the trucks, the smuggled cigarettes were quickly distributed to retailers in towns. Distribution was fast, normally done within 4 hours after loading was completed, and they were sold like any other cigarettes at similar retail outlets as if duties were paid. There was a case when the cigarettes could not be distributed fast enough because the authority came in too early after receiving tips from their informers. Smugglers tried to hide the cigarettes in a building that looked like a toilet. It caught the eyes of customs

instantly because such a beautiful toilet could not have been in a remote village by the sea. Upon checking, smuggled cigarettes were found hidden there.

If the smuggling is successful, it is likely that the cigarettes do not go straight to the licensed importers or wholesalers.[20] To avoid detection by the Customs, the smuggled cigarettes are first stored in empty houses or illegal stores, located at palm oil estates or in remote villages. From these stores, the smuggled cigarettes were delivered to the retailers in a normal way, carried in vans owned by the wholesalers, passing as duty-paid cigarettes. The cigarettes could well be sold as smuggled ones, normally at slightly cheaper prices compared to DP cigarettes.

The smugglers too had their own informers who could be the people from the customs department or the police. No one knew exactly who they were and it remained mere speculation. But often times anti-smuggling raids were unsuccessful, as if the smugglers knew that the raids were going to take place. To avoid detection, customs had to devise different ways and to avoid simply playing hide and seek all the time.

Another step taken by the customs is to carry out codenamed operations, one such operation "*Operasi Pemutihan*" (translated means *Whitening Operations)* was conducted recently. Accordingly, customs established permanent camps in places where smuggled cigarettes are normally landed which are manned by their own staff. This could be quite expensive, especially if speed boat patrols have to be done continuously.

[20] One of the names of the licensed importers was given as Lady Juta suspected of involving in active smuggling.

7.0 ESTIMATES ON THE AMOUNT OF SMUGGLED CIGARETTES

The estimates on the amount of smuggled cigarettes into Malaysia tended to vary. The New Sunday Times published a report saying that smugglers were capitalizing on poor enforcement at the country's major ports, bringing in contraband and counterfeit cigarettes that cost the Government about RM1.2 billion (US$315,789,474) in unpaid duties.[21] However, WHO estimated that tobacco smuggling in Malaysia results in around US $200 million (RM760 million) in tax loss each year.[22] The Director General of Customs latest estimates indicated that Malaysia is losing around RM1.1 billion (US$290 million) of unpaid duty every year, mostly due to escalating smuggling activity.[23] According to the cigarette industry, contraband and counterfeit cigarettes accounted for 21% of the market share. The industry's findings reveal that smuggling has also increased from 9% in 1994 to 21% in 2002[24].

The situation in Sabah and Sarawak is worse. The newspaper quoted one of the Cabinet Ministers as saying that 80% of the cigarettes sold in the two states are either contraband or counterfeit.[25] This compares with the tax from cigarette sales of about RM1.2 million (US$315,789) per year as indicated by the tobacco industry.[26] As an estimate of sales, it has been said that past decade showed legal sales stuck in a range between 17 billion and 20 billion sticks. Sales of smuggled cigarettes, by contrast, may have doubled in the past four years to over four billion sticks.[27] The DNP cigarettes roughly make up 12% of the total cigarette market.[28] While the values indicated above were quoted at different time periods, they nevertheless demonstrated the seriousness of the cigarette smuggling in the state.

There seems to be contrasting information on the amount of smuggled cigarettes. The amount of cigarettes being smuggled quoted by the media seemed to be bigger than the amount given by the customs. To begin with, the smaller amount of cigarettes confiscated by the customs did not truly represent

[21] New Sunday Times, July 6, 2003.
[22] www.cdc.gov/tobacco/who/malaysia.htm
[23] The Star, June 19, 2004.
[24] New Straits Times, July 8, 2003.
[25] New Straits Times, July 8, 2003.
[26] The New Straits Times, November 26, 2000.
[27] Wall Street Journal, November 15, 2000.
[28] The Star, Monday, August 17, 1998

the actual amount being smuggled each year, because customs were not able to trace and arrest all smuggling attempts. The vast areas of the shores of Malaysia where smugglers can possibly land their goods make it impossible for customs to trace every single attempt. Similarly, it would be difficult (while not necessary for transshipment goods) to examine every single container of non-taxable goods that passes the country's ports.

As Table 3 below indicates, since 1999, customs had been successful in confiscating between ten and twenty million Ringgit worth of cigarettes attempting to be smuggled into Malaysia, with the exception of 2002 when the amount reached over RM20 million. This is rather small compared to the amount reported by the press. Certainly, the amount is far less than the reported 12% of the total cigarette market. The success in 2002 is also reflected in the seizure for whites, which recorded a value of RM13.8 million. The statistics clearly indicates that by chance customs has been more successful to seize kretek than whites across the years recorded here. However, there was no added effort given to either whites or kretek in the exercise to combat smuggling. Since taxes are the same for all types of cigarettes, there are no special incentives to smuggle more kretek than white cigarettes.

The percentage of smuggled white cigarettes compared to sales of similar cigarettes is shown in Table 4 below. The percentage is absolutely small, between 0.3% to 0.7%. However, as noted earlier, these figures might not represent the actual amount of white cigarettes being smuggled into the country since customs did not confiscate every successful smuggling attempt.

The seizure of cigarettes does not necessarily mean that the smugglers were arrested either. Thus far, no one was arrested for smuggling cigarettes. The smuggled cigarettes could have been confiscated at illegal stores or unoccupied houses situated in palm oil plantations or in remote villages, after receiving information from customs sources. Based on information that the customs had received, they had in the past actually stopped trucks suspected of carrying smuggled cigarettes. The cigarettes were confiscated if no sufficient evidence showed that relevant taxes had been paid. But the truck driver could not be arrested since he normally claimed to be working under directive of his owner, and many a times, even if the truck drivers were brought to court, the customs lost due to lack of sufficient evidence that they were the smugglers. There were a few cases of arrests and customs could provide sufficient evidence in court. The cigarettes were then confiscated and the trucking companies were compounded with fines up to the maximum of RM5, 000 (US$ 1,315.79).

According to the customs, the amount of fines was rather insignificant to the smuggling syndicate, judging from the amount of money they could have made if the smuggling was successful. The odds were very much in their favor, and therefore, they did not mind paying the fines. As indicated earlier, such a small amount of fines under the law is easily compensated by the profit they get from successful smuggling attempts. If the smuggling was successful, everyone in the chain would make some money, and this could be enough motivation for them to continue smuggling.

TABLE 3
QUANTITY, VALUE AND ESTIMATED DUTY FROM SMUGGLED CIGARETTES (1999-2003)

YEAR	Quantity (Kg) Confiscated	Kretek				Quantity (Kg) Confiscated	Whites			
		Value		Estimated Duty			Value		Estimated Duty	
		RM	USD	RM	USD		RM	USD	RM	USD
1999	202,451.2	12,703,863	3,343,122	4,580,653	1,205,435	53,630.45	2,638,881	694,442	7,375,831	1,941,008
2000	133,003.6	8,445,214	2,222,425	29,138,688	7,668,076	95,056.99	6,215,682	1,635,706	20,506,341	5,396,406
2001	195,006.5	13,315,376	3,504,046	48,397,862	12,736,279	19,385.90	1,413,726	372,033	4,386,024	1,154,217
2002	200,531.19	13,908,689	3,660,181	57,112,251	15,029,540	177,149	13,821,307	3,637,186	29,029,532	7,639,351
2003	180,802	12,043,255	3,169,278	52,997,789	13,946,787	108,968	7,782,830	2,048,113	25,047,579	6,591,468

Source: Royal Customs of Malaysia

Table 4
QUANTITY (kg) OF SMUGGLED WHITE CIGARETTES AS A PERCENTAGE OF SALES

Year	Smuggled*	Sales**	%
1999	53,630	15,504,000	0.35
2000	95,057	27,271,000	0.35
2001	19,386	25,618,000	0.08
2002	177,149	23,079,000	0.77
2003	108,968	23,971,000	0.45

*Source: Royal Customs Department, Malaysia
**Source: Monthly Manufacturing Statistics, Kuala Lumpur: Statistics Department Malaysia, November, 2005.

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8.0 MEASURES TO CURB CIGARETTE SMUGGLING

One of the weaknesses in the present customs clearance system of cargoes is the inability to examine every single container that leaves the port, especially if it has been declared as transshipment goods. These goods, by law, need not be examined. For example, some imported input materials for production are exempted from tax. What the smugglers have to do in the case of smuggling of contraband whites is simply to file the declaration that the goods are for transshipment to a third country, or declare them as non-taxable items required for production. Iron bars for construction are the case in point.

The dilemma on the part of customs is whether or not to examine each container box that goes through the port. Even if they decide to examine every box that comes in or leaves the port, this exercise is quite meaningless, especially if those boxes are declared as either materials for production or transshipment goods. A thorough examination of the boxes which are declared as materials for production will take a long time, and would unnecessarily cause a delay to the manufacturers, who most of the time adopt the Just-in-time inventory system. In this manner, if smuggled cigarettes are declared as goods in transit or materials for production, more often they will not be examined. This is like a loop-hole in the system.

Because of the pressures from many quarters on the customs that they have to examine as many boxes as possible, the department bought scanning machines to determine the content of the containers. According to the customs officials, these scanners are quite accurate in displaying the visual of the contents of the container boxes. They enable them to open up the boxes once the visuals look like taxable items such as cigarette cartons. Four more of such machines were purchased to bring the total to 12, and these were installed at Port Klang in Selangor, Port of Tanjung Pelepas and the port of Pasir Gudang in Johor, Kuantan, Pahang, Penang, Sabah and Sarawak. [29]

In addition, the banderol tax label system was used for imported cigarettes while locally-produced cigarettes would have security ink marks. This was scheduled to be implemented in April 2004[30] but was finally implemented in May 2004. By these systems, cigarette importers are required by law to append

[29] Utusan Online, May 3, 2004.
[30] Banderol and Security Ink were both implemented in May 2004.

the banderol to every pack of cigarettes to be exported to Malaysia, while cigarette manufacturers in Malaysia would have to stamp security ink marks on every pack of cigarette manufactured, under the Customs supervision. These measures arose from the extent of smuggling, including cigarettes, had reached a sizeable proportion. These systems would enable Customs to establish if duty on particular cigarettes in the market had been paid. However, customs were required by the Government to examine the effectiveness of the systems from time to time, to see if they had been abused.

The first proactive measures undertaken by the customs is perhaps to set up a Customs Intelligence Centre located at the Customs Headquarters in Putra Jaya, which would be able to intercept and review the declarations made electronically at the country's major ports. The unit would be able to detect customs fraud such as falsified declarations and involvement of certain groups in such activities, not discounting the possibility of Customs staff being involved in such frauds. Action will be taken against such personnel if they are found guilty.

Customs would also organize more information sessions and mount anti-smuggling campaigns to make people more aware of the danger of smuggling. Information from the public is sought and rewards are indicated if they lead to the arrests of smugglers. Above all, the customs admit that the fines for smuggling are absolutely too small and insignificant to stop the activity. Measures are being undertaken to step up the fines until they are effective enough to stop smuggling. But customs does not know when the new law will be passed for enforcement.

In their latest effort to stop smuggling, the customs is targeting the smokers themselves, especially those who buy and smoke smuggled cigarettes. "Under a new move by the Customs Department to combat the smuggling of cigarettes, smokers could be fined RM100 (US$26) a pack if they are caught buying the contraband. A further deterrent, they would be fined RM2,000 (US$263) for a second offence and charged in court if they commit the offence for a third time, with a fine and a possible jail term of up to two years"[31]

In addition, customs would now go to public places like shops, restaurants and other food outlets, entertainment places like night clubs, and five-foot ways to check locally-manufactured cigarettes without security inks. This also applies to imported cigarettes which could have been wrapped up in banderol tax label

[31] The Star, June 19, 2004.

on the boxes to indicate that relevant duties have been paid. If smokers are found with boxes without either of one of these identifications, they will be arrested.

Smokers, distributors, suppliers and retailers were given one month grace period to get rid off cigarettes without identifications or smuggled cigarettes. Compared to smokers, suppliers would face a heavier penalty of RM100, 000 (US$26,300), which is 10 to 20 times the duty of smuggled cigarettes, or they would be liable to be jailed for up to three years or both, under the law.

9.0 CONCLUSIONS

Rather unexpected and interesting like the above findings is the role of Singapore in cigarette smuggling into Malaysia. While Indonesia has been implicated as the main source of illegal kretek, Singapore is not expected to be implicated as an important neighbor that plays a direct role in cigarette smuggling, by virtue of it being a transshipment port.

Despite the high awareness on the existence of cigarette smuggling, the authority has not been successful in stopping and abolishing the activity. It will be years before the results of the new customs measures (such as the use of scanners) will be known and understood.

Customs are fully aware that smugglers are smart people, who would counteract any measures taken by the government. They are likely to outsmart the customs, especially if they get the support of insiders from the department itself. Customs believe that part of the failure to curb smuggling is due to the some of the officers themselves who have been paid to give information pertaining to customs activities to the smugglers. If such information lead to successful smuggling, customs would have been offered RM30,000 (US$7,800) per truck of smuggled cigarettes. With approximately five trucks for every successful smuggling attempt, the reward is substantial for an ordinary customs officer.

To fully implement the measures to detect fraud is essentially an impossible task. It involves the Customs Law itself, which people outside the department would not understand. Realizing that smuggling hurts revenue, customs is going all out to curb the activity and to identify the black sheep that act as informers to the smugglers. On the softer side, customs is also inculcating integrity among its officers through training and orientation programs. The harder side of the law, including enforcement and stronger penalties, could be more effective in controlling cigarette smuggling.

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About SEATCA

The Southeast Asia Tobacco Control Alliance (SEATCA) works closely with key partners in ASEAN member countries to generate local evidence through research programs, to enhance local capacity through advocacy fellowship program, and to be catalyst in policy development through regional forums and in-country networking. By adopting a regional policy advocacy mission, it has supported member countries to ratify and implement the WHO Framework Convention on Tobacco Control (FCTC)

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