

# ‘THE DRAGON BREATHES SMOKE’

## *Cigarette Counterfeiting in the People’s Republic of China<sup>1</sup>*

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### **Abstract**

This article aims at providing an account of the social organisation of the cigarette counterfeiting business in the People’s Republic of China; a business that has been feeding the cigarette black markets around the globe. Specifically, we aim to exhibit the scale and nature of cigarette counterfeiting in mainland China, describe the practices and actors in the different phases of the trade, and examine the role of corruption and violence in the particular business. We argue that cigarette counterfeiting is one of the side-effects of China’s reform and ‘opening up’ policy, and a feature of the country’s economic development process.

**Keywords:** counterfeiting, cigarettes, China, illegal market

### *Introduction*

The illegal trade in tobacco products is a phenomenon that only recently has gained some prominence and despite the fact that it has a much longer history. There are three main schemes characterising this trade in the last two decades: a) *bootlegging* - buying an amount of cigarettes that exceeds custom regulations; b) *Large-scale smuggling* - of untaxed cigarettes diverted from licit international trade, and c) *counterfeiting* – or the manufacturing of fake brand cigarettes (Joossens, 1999; von Lampe, 2006). This article focuses on the third scheme and aims at providing an account of the social organisation of the counterfeiting business in the People’s Republic of China (hereafter China), generally believed to be the main source for counterfeit cigarettes worldwide. According to recent estimates, up to 400 billion counterfeit cigarettes are produced in China per year (Chen, 2009; Joossens *et al.*, 2009), representing roughly the number of cigarettes (legal and contraband) consumed in the UK over a six-year period. China has criminalised cigarette counterfeiting through a net of general and specific laws and regulations. Section 140 (chapter 3) of the *Chinese Criminal Law* of 1997 has made the production and trade of counterfeit goods in general an ‘Offence that Undermines the Socialist Market Economy’ punishable by a range of possible sentences from fine to life imprisonment. In addition, the *Chinese Law of Tobacco Exclusive Sale* stipulates that legal traders who sell counterfeit tobacco products must be fined at 50% of the market value of the counterfeit products seized. There are also a number of regional and local legislations, and administrative regulations governing cigarette counterfeiting such as the *2003 Jiangsu Provincial Council Resolution of Tobacco Exclusive Sale Management*.

There is a wide perception that cigarette counterfeiting in China has been increasing and that no part of mainland China has remained immune from such activity. Governmental agencies, media and tobacco manufacturers portray cigarette counterfeiting – just as other illegal tobacco-related activities - as the business of serious ‘organised criminals’ and of threatening ‘criminal organisations’ (Chow, 2003), and a pessimistic picture has been painted

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by the authorities as far as measures against the cigarette counterfeiting business are concerned. At the National Anti-Cigarette Counterfeiting Conference held in 2008, Zhang, the Deputy Chief of the National Tobacco Exclusive Sale Bureau pointed out:

*“...the situation of cigarette counterfeiting in China is severe. In the hot spot areas cigarette counterfeiting has not been attacked effectively. Counterfeiting networks are operating. Materials are re-supplied after the law enforcement crackdowns, and there is smooth and frequent counterfeit cigarette distribution...Cigarette counterfeiting cannot be solved essentially within a short period of time so we cannot be over-optimistic...and should be prepared for the longer term battle against this illicit activity...”* (Zhang, 2008).

China's leading role in cigarette counterfeiting cannot be understood without considering the broader social and economic importance of tobacco in this country. China has the largest smoking population in the world reaching approximately 300 million or one third of the world smokers (Tobacco Free Centre, 2009). It has also been suggested that Chinese smokers spend 3% of per capita GDP on tobacco (Wang, 2006; Hu *et al.*, 2005), often at the expense of other, more vital commodities and services (Hu *et al.*, 2008). This huge market has traditionally been supplied almost exclusively by domestic sources. Until recently, foreign cigarettes accounted for only an extremely small share of the legal market (e.g. only 0.8% from 1995 to 1999) as a result of high tariffs on cigarette imports (Hu and Mao, 2002). It was not until 2004 that these tariffs have been substantially lowered (Euromonitor International, no date). These barriers to imports, it seems, have encouraged the smuggling and counterfeiting of foreign brands. In fact, there is some evidence that the counterfeit business has profited from expertise originally acquired from smuggling Western brand cigarettes into China during the 1990s (Chen, 2009). Given the alleged corporate involvement (Lee & Collin, 2006) one could say that China's counterfeit business of today in a way is the sorcerer's apprentice of the Western tobacco industry.

Given the size of its domestic market it is not surprising that China is the biggest tobacco producer in the world, but also one of the most important exporters of cigarettes (Onder, 2002).

The tobacco industry is an extremely important economic sector in China. Organised as a state monopoly, it contributes significantly to the Chinese economy and provides substantial revenues for the central government and local governments, although at a declining rate (Hu *et al.*, 2009; Wang, 2006). In 2005, 7.6 % of the central government's total revenue came from a combination of tobacco taxes and monopoly profits, compared to 11.4 % in 1995 (Hu *et al.*, 2009). Because local governments receive their share of revenues primarily from taxes on tobacco leaves rather than on cigarettes they have an incentive to encourage farmers to increase the production of tobacco beyond set quotas, thus creating a source of raw tobacco for the manufacturing of counterfeit cigarettes (Hu *et al.*, 2007; 2009).

Tobacco provides income for millions of Chinese people. According to Wang (2006), 4.1 million rural households are involved in the cultivation of tobacco, and five million (licensed) tobacco selling points create job opportunities in the private sector. The manufacturing industry, however, is less significant in this respect. Wang (2006) gives a recent figure of only 215,600 workers involved in the (legal) production of cigarettes, marking a continuous decline. Since 2001, when China joined the WTO, the administration has pursued an aggressive agenda to restructure the tobacco industry. The aim has been to establish a small number of large-scale tobacco enterprises with an ability to compete against major international brands. In the process, numerous small and inefficient factories have been closed down (Euromonitor International, 2008; Hu *et al.*, 2009). One apparent consequence of the restructuring of the legal tobacco industry is that a sizeable workforce of skilled

labourers as well as production machinery has been made available for the illicit tobacco business.

A third historically developed characteristic of the Chinese tobacco industry may have contributed to the emergence of large-scale illegal cigarette trading: the high level of regulation. As indicated, despite China's shift to a market economy thirty years ago, the tobacco industry in the country is highly regulated by the central government, and specifically the *State Tobacco Monopoly Administration* (STMA). The state company under the title *China National Tobacco Corporation* (CNTC) and a number of smaller companies (such as *China Cigarette Sales & Marketing Corporation* and *China Tobacco Materials Corporation*) are subjected to this authority. The regulation provides numerous impediments to individual entrepreneurs wishing to be involved in the legal business. Specifically, a Permit of Exclusive Sale of Tobacco is required before a legal tobacco selling business can be opened, a procedure which is lengthy and difficult because these legal requirements and processes are sometimes affected by corruption (see Caijin, 2008). The formidable difficulties involved in obtaining a tobacco exclusive sale permits, it seems, in part account for the existence of the illicit cigarette business.

Of great relevance to this study is the cultural meaning of cigarettes (and other tobacco products) in Chinese society. Tobacco is a commodity that is often associated with success and affluence, and has been used as a lubricant of social relationships and an 'instrument' of bribery (see Tomson and Coulter, 1987). Particularly, international and Chinese expensive brands of cigarettes have been traditionally purchased as gifts, for example, on important occasions. In fact, counterfeit production and sales are said to peak around the New Year and spring festival celebrations (China Daily, 2004).

Another aspect, defining the broader environment under which the illegal cigarette business flourishes in China, is the global demand for cheap cigarettes. Since the late 1990s, large quantities of counterfeit cigarettes from China have been introduced to illegal cigarette markets around the world, thus rendering China an important node in the global illegal tobacco trade. Although there are indications that the production of counterfeit cigarettes has increased in other Asian countries and Eastern Europe as well as Germany and UK (see von Lampe, 2006), China remains the major source country for this particular commodity (Chen, 2009; SOCA, 2009). However, although there is a considerable amount of publications on tobacco and health issues, tobacco economics, and the complicity of tobacco manufacturers in the illegal tobacco trade in China, there is comparatively little being published on the social organisation of the cigarette counterfeiting business in the country. This perhaps reflects the relatively slow development of criminology in China, and Asia in general, compared to the western world (see Liu, 2009; 2008). Our aim is to contribute to the research on the cigarette counterfeiting business in China. Specifically, we aim to: (a) describe the scale and nature of cigarette counterfeiting in the mainland China; (b) discuss the practices and actors during the different phases of the trade; and (c) examine the role of corruption and violence in cigarette counterfeiting. We argue that cigarette counterfeiting is one of the side-effects of China's reform and 'opening up' policy, and a feature of the country's economic development process.

### *Data and Methods*

As noted above, there is very little empirical research and evidence on illegal cigarette-related activities including cigarette counterfeiting in China. Various researchers (e.g. Heimer & Thøgersen, 2006; Liu, 2008) have identified the historical, cultural and political obstacles in attempting to conduct *empirical* criminological research in China. Criminological research was openly forbidden in China for 27 years prior to 1979 (Bakken, 2000). But even after

1979 research has been suffering from what Klein and Gatz (1989: 175) call “bureaucratic inflexibilities”. Public officials are not encouraged to disclose information about crime-related matters; neither are they willing to express their personal views on any potentially sensitive matter which may jeopardise the image of the agency they work for or the state. There is the general problem that there are few incentives for criminal entrepreneurs to participate in research interviews. This is even more the case in China, where criminals have been traditionally seen as the ‘enemy of the state and its people’ (Davies & Shen, 2009). There are *technical* restrictions for Chinese and non-Chinese researchers as well: there are 34 provinces, autonomous regions, municipalities and special economic zones in China. Combined with the wide dispersal of the population, there are ethnic differences and an extremely diverse context, which does not allow generalisations to be made when researching one area, while financial costs make empirical research in all areas an even more difficult endeavour. In addition to these impediments to prospective research, these geographic and demographic features, along with the circumspect attitude of the Chinese state, have ensured that statistical information is not collected and disseminated by the Chinese bureaucratic apparatus, at least to the extent of other countries (Brewer *et al.*, 1996).

Therefore, the information supporting this study is drawn from open sources. Open sources have been used in previous works on illegal tobacco trade in general (see von Lampe, 2006). Apart from a general literature and internet search, we searched the news reports from the website of *Xinhua Ribao* – one of China’s major official newspapers (<http://www.news.cn>) by using the keywords ‘cigarette counterfeiting’. We obtained 381 cigarette counterfeiting-related news articles which were collected from a variety of online sources from 11 May 2001 to 22 September 2009. We also conducted a random online search by using the keywords ‘cigarette counterfeiting in <name of province>’. The purpose of this was to obtain cigarette counterfeiting cases detected in the provinces that are not included in the *Xinhua* database. This search added another 106 news articles to our database.

The cases we have cited in this paper are drawn from the news articles carefully selected from our initial search. Through the initial search, we also identified a handful of surveys conducted by journalists from newspapers such as *Caijun Ribao*, *Shichang Bao* and *Chengshi Wanbao*. Likewise, a large amount of data was collected from a tobacco-specialised website, namely *Tobacco China* (<http://www.tobaccochina.com>). In addition, we searched all China’s tobacco authority official websites, including the website of the *National Tobacco Exclusive Sale Bureau* (NTESB) which has published annual reports from 2003 to 2008. These reports contain statistics on (a) the number of cases detected, (b) the number of counterfeiting sites, (c) the number of rolling machines seized, (d) tons of tobacco leaves seized, (e) the number of units of cigarettes seized, and (f) the number of people arrested and sentenced for cigarette counterfeiting from 2002 to 2007.

The sources were carefully selected in order to cover cigarette counterfeiting in *all* provinces of mainland China. The reason why the data we use for this study do not include Hong Kong, Macao and Taiwan is because they constitute special administrative and – primarily- economic zones that have adopted different policies and practices. Overall, these three areas are discernibly different from mainland China in terms of their historical, socio-political and economic features.

The fact that the first author of this article is of Chinese origin and can read Chinese provided us with the opportunity to use sources that are not easily accessible by westerners. On the other hand, the sources we have used refer to only those cases which the authorities came across thus ignoring cases of successful counterfeiters. There is a possibility, therefore, that the official and media accounts are biased towards the least successful counterfeiting schemes, and may also be presenting the issues relating to the actors of the counterfeiting business in a sensational and morally charged manner. Although China is hardly an exception

to the sensational manner in which crime is treated in official and media accounts, Zhong (2009: 109) has already argued that official, media and even academic accounts in China “are replete with language of strong moral flavour, in line with the strongly moralistic quality of the whole society”. We note here that we have not adopted our sources’ representations of the entities involved in the business; we only use the purely ‘technical’ information to make inferences. Finally, we acknowledge that besides the ‘standard’ limitations of official data there are a number of China-specific issues relating to criminal statistics. Apart from the fact that data are not readily and widely available, the little data that are available to researchers is impossible to assess due to lack of knowledge of or ambiguity about the data collection procedures as well as due to conscious practices on the part of the authorities to manipulate data towards serving their hidden agendas and meeting their political or other objectives (Bakken, 2005). Despite the limitations of these data however, we think they are worthy of examination.

### *The scale of the cigarette counterfeiting business in China*

NTEBS annual reports (NTEBS 2003; 2004; 2005; 2006; 2007; 2008) and China Tobacco Market (2009) provide some data on cigarette counterfeiting in China for the period 2002-2008 (see Table 1). Within this period 1,492,814 cases became known to the Chinese authorities. The year with the largest number of cases detected was 2005 (347,000 cases). The number of counterfeit cigarette production sites that were found by the authorities for the particular period was 22,248, whereas 8,849 rolling machines used for the production of counterfeit cigarettes were seized along with more than 84 tons of tobacco leaves. Overall, 30,825 individuals were arrested for cigarette counterfeiting, 10,742 of whom were sentenced.

**Table 1.** Data relating to cigarette counterfeiting in China, 2002-2008

Year	Number of Cases Detected	Number of counterfeiting sites	Number of rolling machines seized	Tons of tobacco leaves seized	Units (Jian) <sup>3</sup> of cigarettes seized	Arrests (sentenced)
2002	320,000	2,476	1,375	13,000	497,000	4,075 (1,076 sentenced)
2003	220,000	2,575	1,531	-/- <sup>4</sup>	530,000	3,539 (956 sentenced)
2004	269,000	2,805	1,890	-/- <sup>5</sup>	687,000	4,215 (1,208 sentenced)
2005	347,000	2,908	1,608	12,000	730,000	5,336 (1,697 sentenced)
2006	330,000	4,296	1,281	10,600	907,000	6,634 (2,313 sentenced)
2007	5,505 <sup>6</sup>	3,876	717	28,000	928,000	7,026 (3,492 sentenced)
2008	1,309 <sup>7</sup>	3,312	447	20,800	830,000	-/- <sup>8</sup>

<sup>3</sup> One unit (Jian) contains 50 sleeves of cigarettes (=10,000 sticks).

<sup>4</sup> No information available.

<sup>5</sup> No information available.

<sup>6</sup> This figure includes only the cases involving counterfeit cigarettes of monetary value of more than 50,000 Yuan (approximately £ 4,480).

<sup>7</sup> This figure includes only the cases involving counterfeit cigarettes of monetary value of more than 500,000 Yuan (approximately £44,800).

2002-2008	1,492,814	22,248	8,849	84,400	5,109,000	30,825 (10,742)
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Source: NTESB (2003; 2004; 2005; 2006; 2007; 2008); China Tobacco Market (2009).

The aforementioned official statistics possess a number of limitations in addition to the ones relating to the lack of knowledge of or ambiguity about the data collection procedures. The superficial and at points incomplete figures presented above do not provide a picture of the actual extent of cigarette counterfeiting in China, but only those cases that the Chinese authorities have come across. The ‘dark figure’ may be considerable and the seized counterfeit cigarettes, as an official in one particular case is quoted as saying, may constitute “only the tip of the iceberg” (Shichang Bao, 2006). Data on 2007 and 2008 refer to cases involving merchandise of monetary value of more than 50,000 and 500,000 Yuan, respectively, which automatically excludes ‘smaller’ cases. In addition, as is obvious, there have been increases and decreases in the number of cases as well as in the number of seized cigarette packs that do not allow for a possible trend to be discerned at least within these years. But even when trends could indeed be discerned, these could refer more to ‘contextual variables’ (von Lampe, 2004) such as the level of intensity of law enforcement or resolution of the government.

### *The production of counterfeit cigarettes*

Counterfeit cigarette manufacturing and trading originated from the southern coastal provinces of mainland China, Fujian and Guangdong, which borders Hong Kong and Macao. Particularly Yunxiao (Fujian province), and Chaoshan and Guangzhou (Guangdong province) are notorious for the production of counterfeit cigarettes. However, in recent years, due to the centrally-coordinated operations persistently carried out to curb cigarette counterfeiting in these areas, a number of counterfeiting businesses have been displaced to inland China. The counterfeit cigarette production phase can be divided into three stages: (a) acquiring raw materials, (b) manufacturing counterfeit cigarettes, and (c) packing counterfeit cigarettes.

#### *(a) Acquiring raw materials*

In China, counterfeit cigarettes can be produced from tobacco of various levels of quality, second-hand tobacco or even waste. Some of the chemicals which are used to process the low quality tobacco, such as sulphur and carbamide, are poisonous and may cause health problems to cigarette consumers.<sup>9</sup> Low quality tobacco, directly and regularly bought from tobacco farmers, is usually used to make counterfeit cigarettes. Poor quality tobacco includes the totally unprocessed raw tobacco and musty/rotten tobacco which has to go through a process with sulphur and carbamide in order to look better (see Chongqing Chenbao, 2002).

Counterfeiters obtain their tobacco from ‘irregular’ channels as well. In a case that the authorities came across in Shenyang (Liaonin province) counterfeiters used dumped materials and ‘lajiyan’ (‘rubbish tobacco’) to make cigarettes. In addition, the counterfeiters disguised themselves as professional recyclers and bought damaged packaging, ‘unusable’ wrapping paper and unsellable cigarettes from legitimate cigarette companies. Simultaneously, they employed ‘workers’ to collect cigarette butts from the rubbish bins (Shidai Shangbao, 2002).

<sup>8</sup> No information available.

<sup>9</sup> Toxicological research suggests that counterfeit cigarettes expose smokers to heavy metals to a greater extent than authentic cigarettes produced by authorised manufacturers (see Pappas *et al.*, 2007).

In some cases counterfeit cigarettes are also made of non-tobacco waste such as sawdust, wood shavings and rotten vegetable leaves. In such cases, the cigarette wrapping paper, filters and other material are collected from the waste sites (see, for example, Hangzhou Ribao, 2003). In the municipality of Chongqing, rotten vegetable leaves were dried and processed with sulphur in order to be used instead of tobacco in counterfeit cigarettes (Chongqing Wanbao, 2002). It is not unusual, however, for counterfeit cigarettes to be made of good quality tobacco. Mr. Li Yang from the Central Inspection Team of the Beijing Tobacco Exclusive Sale Bureau commented that in some cases “the counterfeit cigarettes intercepted are of good quality. Consumers can hardly tell the difference between these counterfeit cigarettes and the genuine ones” (China News Agent, 2002).

*(b) Manufacturing counterfeit cigarettes*

The actual manufacturing of counterfeit cigarette requires rolling machines. In the past, purchasing cigarette rolling machines was extremely expensive. In order for costs to be cut down, counterfeiters bought used rolling machines from state-owned cigarette factories. The cost of these machines ranged from 600,000 to 1 million Yuan (approximately £ 53,000 to 89,000) per piece. In recent years some machinery manufacturers have started to make copycat cigarette rolling machines, and the price has dropped significantly to around 200,000 Yuan (approximately £ 18,000) per piece. Inevitably, the costs of cigarette manufacturing have been reduced accordingly. With the development and expansion of the cigarette counterfeiting businesses, counterfeiters, like their legitimate counterparts, have started to invest in more advanced equipment. Prior to 2004 only 30% of the cigarette machines seized were automatic whilst currently the counterfeit cigarette production line is 90% automatic (Nanfang Ribao, 2009).

*(c) Packing of counterfeit cigarettes*

Packing is an integral part of the counterfeit cigarette production process. There are legal and illegal enterprises, which specialise in packing only. The district of Guangzhou (Guangdong province) is believed to be the largest counterfeit cigarette packing centre in China. The packing only ‘schemes’ usually operate at a relatively small scale. In Beijing a cigarette packing ‘factory’ operated in a warehouse with only ten to twenty workers, who were manually packing loose cigarettes into the packaging of different popular brands (China News Agent, 2002). Different methods are used for the packing of counterfeit cigarettes in order for consumers to be deceived and detection to be avoided:

- *‘Pick ‘n’ mix’* – genuine cigarettes are mixed with counterfeit ones in each pack. In a Changsha (Hunan province) case, ‘Baisha’ cigarettes of this type were found. Inside the pack there were only seven genuine and thirteen fake cigarettes (Shangbao, 2002). However, this packing method appears to be rare in the cigarette counterfeiting business.
- *Genuine packs* – counterfeit cigarettes are packed in used *genuine* packaging. This guarantees that health warnings are not misspelled, images are clear and other giveaways are not present.
- *Counterfeit packs* – counterfeit cigarettes are placed in packaging resembling that of genuine brand cigarettes. The quality of counterfeit packs appears to have substantially improved from rather primitive beginnings in the 1990s, making it difficult nowadays to distinguish counterfeit from genuine cigarette packs (HM Treasury, 2004).
- *Unique format of counterfeit packs* – In order to attract prospective customers’ attention, some unique packaging is designed for counterfeit cigarettes of the most popular brands, which may not even exist for the genuine cigarettes. In Tianjin, the

gift boxes of 'Zhonghua' cigarettes were sold in the market. Each box consisted of one sleeve of soft pack 'Zhonghua' cigarettes, one hard-pack, one pack of 12 low-tar cigarettes and one pack of super-class 'Zhonghua' cigarette along with an ashtray and a lighter. The gift boxes looked elegant and delicately made and a lay person could not tell they were faked; however, the state-owned 'Zhonghua' cigarette company had never offered this type of gift boxes (Xinhua Net, 2008).

#### *The venues of counterfeit cigarette production and packing*

There is a large and diverse set of venues used for the production of counterfeit cigarettes. These include legitimate factories producing other commodities, warehouses, farms in rural and semi-rural areas, martial arts training schools, temples and private homes. A number of illicit production facilities have also been discovered in underground chambers and in mountain caves. As investigative journalist, Te-Ping Chen, reports that in Yunxiao factories are frequently hidden in dim, bricked-in facilities underground, accessible only via trapdoor and ladder, with the turf masking the tobacco scent (Chen, 2009; HM Treasury, 2004).

#### *The sale of counterfeit cigarettes*

Medium and large quantities of counterfeit cigarettes are sold in shopping centres, department stores, hotel-owned luxury shops and various legitimate small businesses such as groceries and kiosks. Most of these premises are licensed cigarette retailers that sell counterfeit cigarettes as well. For example, in a case in Fuzhou, a legitimate cigarette store displayed legal cigarettes on the shelves and counterfeit cigarettes (as well as smuggled foreign brands) were wholesaled (Fuzhou Wanbao, 2002). There is also, as was mentioned earlier, a large (and increasing) number of floating street-sellers, who trade counterfeit cigarettes outside night clubs, discos, restaurants and other night-time economy establishments or along the street and other public space.

Although selling counterfeit cigarettes is a day-to-day routine business to sellers, and counterfeit cigarettes are sold at any time in virtually any public space to any interested customer, there are still preferable localities, venues, seasons and consumer groups that counterfeit cigarette sellers perceive to be ideal. Tourist spots are commonly chosen to sell counterfeit cigarettes because local cigarette brands are part of the tourist smokers' souvenir shopping in China. Tourists do not have knowledge of local brands and – with some exceptions - they cannot easily distinguish the counterfeit cigarettes from the genuine ones (Tobacco China Online, 2002). Other places where a convergence of sellers and potential buyers is guaranteed, such as ports, coach and railway stations, or even on transportation means, are chosen by counterfeit cigarettes sellers.

Counterfeit cigarettes are often sold in village marketplaces. These marketplaces meet the demand of villagers, who have very little disposable income and cannot afford to buy quality, genuine cigarettes. Of great relevance here is the reluctance of legitimate cigarette sellers to trade in cheap legal cigarettes due to the small profit margin and the subsequent reduction or even cessation of production of cheap (or 'low class') cigarettes by authorised cigarette factories. Finally, counterfeit cigarettes are sold outside mainland China, by mainland Chinese peddlers in Hong Kong, Macao and Taiwan (Lo, 2009), and through global illicit distribution channels on North American, European, Australian, Asian and African markets (Chen, 2009). According to an official from Yunxiao, "...the profit of selling counterfeit cigarettes abroad is 500% whilst that of selling them in the internal market is only 200%" (Caijin, 2008).



## *Actors and patterns of cooperation in the cigarette counterfeiting business in China*

The cigarette counterfeiting business requires a degree of sophistication, and management of resources and labour. Towards this end, counterfeiting networks tend to have a naturally defined horizontal ‘structure’. In fact there appear to be independent, autonomous ‘entities’ involved in (a) production of counterfeit cigarettes and (b) sale of the merchandise and a constellation of actors, who are subcontracted in a way, around those two particular stages of the counterfeit cigarette business. In many cases, and in contrast to other contexts, the structures involved in the *production* of counterfeit cigarettes are hierarchical, and this is most probably a result of the fact that the production of counterfeit cigarettes involves someone who owns the (unauthorised) factory or workshop and workers who are employed *by* him. In essence, a counterfeit cigarette factory is almost identical to a legal cigarette factory.

A number of individuals act as intermediaries who assist in the introduction of the merchandise into the market or who identify persons that can be subcontracted by the counterfeit cigarette producers and offer specialised services (e.g. packers, transporters etc.). The presence of the intermediaries was evidenced in many of the sources consulted. Thus once observers of the business move from one stage to the other, they realise that clearly defined structures and management systems along the *overall* counterfeit cigarette business do not exist. What merely exist are individuals or small groups forming temporary collaborations in order for their shared objective, making profit, to materialise. Unfortunately, the available data cannot offer additional information as to how these collaborations emerge in the first instance.

What is also extremely important to note is that in many cases the production phase of the business is ‘demand-based’; counterfeit cigarette production is based upon an order. The persons, who order the counterfeit cigarettes, however, should be viewed as the ‘initiators’, or the initial customers of the business rather than the ‘organisers’ of the process.

There is a range of individuals from various socio-economic and geographic backgrounds, who directly or indirectly engage in the cigarette counterfeiting business in various ways and play different roles in the counterfeiting process, according to competencies and skills. Similar to other contexts (see, for instance, Antonopoulos, 2008), not all actors are present in all counterfeiting schemes, and one actor may assume more than one role. The different roles are as follows:

- *Tobacco farmers*. They provide the primary raw material for the business. They have an incentive to sell their product irrespective of whether the buyer is an illegal entrepreneur since, as was indicated earlier, there is a surplus of tobacco in China.
- *Unauthorised manufacturers*. They have the capital to invest, consider the counterfeiting of cigarettes a lucrative business and engage in running illegal cigarette manufacturing sites. Some of the unauthorised manufacturers are individuals from families with a tradition in small-scale cigarette-making. For example, in Yunxiao, ‘home cigarette-making’ has a tradition since the Qing Dynasty (1644-1912). It was virtually absent from 1949, when the PRC was established, until the late 1970s when it re-emerged as a normal entrepreneurial activity. In terms of the quantities of counterfeit cigarette introduced to the market unauthorised manufacturers are the equivalent to the wholesalers in the non-counterfeit illegal cigarette markets.
- *Intermediaries*. In those cases in which the production of counterfeit cigarettes is based upon demand, it is the intermediaries, individuals who link manufacturers and prospective customers, by collecting orders through their social networks and then placing the order to the manufacturer. Intermediaries also link other participants in the business such as manufacturer and transporters. Intermediaries may not be involved in

the actual manufacture or sale of counterfeit cigarette but are what Morselli and Giguere (2006) call ‘critical actors’.

- *Specialised workers. Former workers of state-owned cigarette factories.* Many workers have been made redundant from the state-owned factories and have been employed by cigarette counterfeiting entrepreneurs particularly in the southern regions of China, such as Fujian, Guangdong and Guangxi provinces (Caijin, 2008). In one of the cases we came across, all 30 workers in a counterfeit cigarette manufacturing site were former workers of state-owned cigarette factories in Hunan and Anhui provinces (Guizhou Dushibao, 2002). These specialised workers who are basically tobacco experts or ‘recipe specialists’ enjoy more benefits than simple workers because of their technical expertise, which is functional for the counterfeiting business. To seek long-term commitment to the illegal enterprise, counterfeit cigarette manufacturers pay relatively high salaries to specialised workers (Caijin, 2008).
- *Packaging producers.* Packing materials, such as boxes, cigarette packs, wrapping foil, plastic wrapping and other packing accessories are produced by individuals and small legal businesses specialised on this part of the process. In some cases authorised and unauthorised cigarette manufacturers are also the customers of the same packaging producers.
- *Trademark and barcode printers.* They make packaging trademarks, barcodes and even counter-counterfeiting fiscal marks available to counterfeiters. In September 2007 a printing workshop was found in Shantou city of Guangdong province, and several printing machines as well as 414,000 empty cigarette packs with printed trademarks were seized (Shantou Ribao, 2007). These services are not necessarily provided by professional printers only; they can also be offered by sole individuals in their own house. Liaoshen Wanbao (2002), for instance, reports the case of a 60-year old woman specialising in spraying barcodes on ‘Zhonghua’ and ‘Xiaoxiongmao’ packs.
- *Non-specialised workers.* These are usually internal migrants - including children - from the countryside, who are used as cheap labour for primarily menial tasks such as cleaning the tobacco, carrying the merchandise from the factory to trucks or other means of transportation or even collecting cigarette butts and packs from rubbish bins and the street to be used for the manufacturing of counterfeit cigarettes. In many cases, these non-specialised workers are introduced to a ‘short migration’ system of work that has been adopted in the cigarette counterfeiting business. This basically entails the workers not being allowed to leave the workshop until the end of their ‘contract’, working in double shifts in operations that run 24-hour a day, and not being allowed to use mobile phones (e.g. Changjiang Yancaobao, 2002). Caijin (2008) reports that a large-scale Yunxiao counterfeit cigarette site was built underground. All workers were taken from the train station to the site in a closed container, so that they would not be aware of the exact location of the site. A person was assigned to shop for necessities for the workers, who would be transported to the train station in the closed container after the termination of their ‘contract’.
- *Warehousemen/storage providers.* Warehouses and other legitimate storage services are used by counterfeiters for storing the merchandise. Some unusual premises have been reported. For example, in one of the cases we came across, a pigsty was used to store counterfeit cigarettes. The front of the pigsty was occupied by pigs and at the back, and underneath the pile of pig food, the counterfeit cigarettes were hidden, while two hunt dogs were guarding the premises (Sichuan Ribao, 2002).
- *‘Security guards’.* To avoid detection of the manufacturing sites, individuals are employed to carry out physical surveillance. In a case in Yunxiao, security guards

were hired to be present at each junction of the country road towards the manufacturing site. These security guards were equipped with walkie-talkies to report any suspicious activities (Caijin, 2008). In another case in Inner Mongolia, cameras were installed above an underground cigarette factory and individuals were hired for the control room (Xinhua Net, 2005).

- *Transporters*. Transporters play a crucial role in the cigarette counterfeiting business from the moment the merchandise leaves the manufacturing site. The ways of transportation for counterfeit cigarettes vary. Locally, counterfeit cigarettes are transported by vans, cars and motorbikes. In Nannin (Guangxi province), a man transported 50 sleeves of ‘Santa’ cigarettes on his motorbike (Nanguo Zaobao, 2002). Nationally, legitimate transport companies, logistic centres and individual (professional or non-professional) lorry drivers are hired by counterfeiters although sometimes the transporters are not aware of the illegal merchandise. In some of the cases transportation companies are set up specifically for the purpose of delivering counterfeit cigarettes. Merchandise is often concealed among other commodities. In Wenzhou (Zhejiang Province), for instance, 298 units of counterfeit cigarettes were disguised as boxes of insoles (Wenzhou Dushibao, 2002). Counterfeit cigarettes are also delivered by air through air-cargo companies. In Guangzhou there were more than ten air-cargo agencies around the airport amongst which eight answered that they would have no problem to deliver counterfeit cigarettes when a fake request was made by a journalist (Nanfang Ribao, 2009). Quantities of counterfeit cigarettes are also transported to markets abroad usually by ship from important commercial hubs in the east and south of the country such as Shenzhen and Shanghai (Caijin, 2008).
- *Sellers*. There are two types of counterfeit cigarette sellers. The first type is the *street-seller*. In most of the cases street-sellers, particularly in urban centres, are internal migrants from the countryside and unemployed city residents. Some of them work as sellers of counterfeit cigarettes parallel to their legitimate (or in some cases illegitimate) job. In one of the cases we came across, a seller used to work simultaneously as a street shoe-repairer. It is also very common for females to be involved in the street sale of counterfeit cigarettes. Increasingly, large numbers of street-sellers act as ‘entrepreneurs’ by depositing a small amount to purchase a number of counterfeit cigarette packs or sleeves. The second type is the *seller operating in legitimate enterprises* and with larger quantities. For example, in Fuzhou (Fujian province), a grocery had a permit to trade in tobacco products. However, along with trading legitimate cigarettes the owners of the business were also distributing counterfeit cigarettes (Fuzhou Wanbao, 2002).
- *‘Look outs’*. The role of ‘look outs’ has been identified in the cigarette black markets of other countries (Antonopoulos, 2008; von Lampe, 2003). ‘Look outs’ ‘patrol’ the area of street-selling and warn the sellers about the presence of uniformed law enforcement agents as well as journalists and TV crews.
- *Corrupt public officials*. Having power, information, and powerful social networks, public officials can be actively or passively involved in the cigarette counterfeiting business.

### *Counterfeit cigarettes business and corruption*

There are basically three forms of corruption of Chinese public officials which relate to the cigarette counterfeiting business:

- (a) *Active engagement* – this is the extreme form of corruption in cigarette counterfeiting, in which public officials take advantage of their power due to their position, specialised knowledge and social networks to establish cigarette counterfeiting manufacturing sites. In an Inner Mongolia (Neimenggu) case, the four owners of a counterfeit cigarette manufacturing site were officials of the local Bureau of Industry and Commerce. One of them was also the former head of the Market Unit in the Fengyuan Bureau of Industry and Commerce (Xinhua Net, 2005).
- (b) *‘Protective Umbrella’* – Public officials may play a role of a ‘protective umbrella’ (*‘baohusan’*) for cigarette counterfeiters. For various reasons corrupt officials protect cigarette counterfeiters and intervene in case cigarette counterfeiters are arrested. This ‘protective umbrella’ allows for the termination of the illegal business to be extremely short-termed and the business virtually uninterrupted, irrespective of the number of detections. As an officer employed in the Shanxi tobacco management authority confessed to a *Shichang Bao* newspaper journalist:

*“There are several illegal cigarette traders in every city of our province, and they all have close relationship with the officials... The dealers and officials have an alliance and they share the illicit profits. Counterfeit cigarette dealers control the counterfeit cigarette markets in Taiyuan and the peripheral cities. When things go wrong, someone would come out and exculpate the illicit dealers from trouble”* (Shichang Bao, 2006).

In another case involving the large-scale production of counterfeit cigarettes, an individual reported the details of a manufacturing site to the local law enforcement agency and obtained his reward. After months the counterfeit cigarette manufacturer was still in business (Caijin, 2008).

- (c) *‘Turning a blind eye’*: public officials may not be directly engaged in cigarette counterfeiting or in providing a ‘protective umbrella’ to participants in the counterfeit cigarette business; however, some of them may ignore the activities of cigarette counterfeiters in exchange for financial rewards. In some cases a financial reward may not even need to be available, and this appears to be the case in relatively small, primarily rural and semi-rural localities in which there are pre-existing social relationships between counterfeiters and public officials.

In this context it should be noted that provincial governments in China are being treated as enterprises by the central government in terms of economic performance and success (see Chen, 2002). Since cigarette counterfeiting, through the use of locally grown raw tobacco, is a source of revenue for the provincial government and provides employment for many individuals, *local* governments seem to be reluctant to crack down on counterfeiting businesses especially when the unauthorised production relates to international brands (e.g. Marlboro, Benson & Hedges) or brands that are not produced in the particular province, and therefore does not cause a conflict of interests with local authorised manufacturers (Yao, 2006; White, 1996). In French’s (2007) words, “it is the froth in the economy that [counterfeiting] creates that counts most, not niceties like intellectual property or fussy product safety details”. It should be noted however, that corruption was not present in all cigarette counterfeiting cases we came across and thus, similar to other contexts, corruption is *not* necessarily to be considered as an essential feature of the counterfeiting business. It is also important to acknowledge that the Chinese government, partly to protect its own brands, partly in compliance with international obligations and aided by tobacco corporations, has

made increasing efforts to crack down on cigarette counterfeiting thereby creating a more hostile environment for cigarette counterfeiters and their facilitators (Hu *et al.*, 2009; Levin, 2003).

### *Counterfeit cigarettes business and violence*

As previous research on illegal markets has shown, violence does not occupy a central part in the business but is a sign of “market dysfunction and instability” (Pearson and Hobbs, 2001: 42). Although violence *is* present in the illegal cigarette business in various contexts (see Antonopoulos, 2008), it does not constitute an *integral* part in the market. This also appears to be the case with the cigarette counterfeiting business in China; however, what can be observed in China is a higher prevalence of violence in the business. Violence and/or threat of violence are directed towards various types of individuals. In China there is a group of people who act as professional informants, they provide information on counterfeiters and counterfeiting activities to the authorities, and they are rewarded for the relevant information they provide. Within this context, gangs are hired by counterfeit cigarette manufacturers to attack law enforcement informants. One of the numerous cases which received much media attention is of Zeng Changsheng and two fellow informants, who used to act as professional informants for the tobacco authority. Zeng Changsheng’s fellow informants lost their lives while he lost one ear, which resulted in him stopping to work for the authorities (Caijin, 2008). An official from Guangdong Provincial Tobacco Exclusive Sale Bureau commented on the killing of the two informants:

*“...it is known that cigarette counterfeiters are using underworld criminal gangs to protect their operations. Once being identified, informants are physically tortured... and even kidnapped. But it is shocking that the counterfeiters were so brutal that they dared to beat informants to death”* (Fuzhou News Net, 2005).

Violence and threats of violence are sometimes used towards law enforcement officials by cigarette counterfeiters. In one of the relevant cases we came across, threatening phone calls were made and text messages were sent to police investigators and some of their family members during the investigation. One of the investigators received more than thirty threatening messages on a single day (Dongya Jinmao News, 2008). Counterfeit cigarette entrepreneurs may also impose violence towards tobacco authority officials and police officers when the actual seizures of rolling machines, raw tobacco and counterfeit cigarettes are carried out (see Jianghuai Chenbao, 2002).

What is perhaps unique in the counterfeit business in China is violence towards buyers. In a recent fatal incident that occurred in Guangzhou, the capital city of Guangdong province, a man was beaten to death by four security guards of a legal establishment in which a shop selling counterfeit cigarettes was located, after he protested about the quality of the cigarettes bought (Xingxi Shibao, 2009). This was one of the incidents that raised serious public concerns about cigarette counterfeiting in China.

The counterfeit cigarette business as a whole and individuals involved in cigarette counterfeiting however, can be victims of violence or threat of violence, and extortion. Sellers, for example, are often robbed of their profits. There are also different forms of extortion from ‘protection fees’ to ‘rent fees’ paid to criminal gangs that allow the continuation of the business. According to Nanfang Ribao (2009), in Wuxianqiao, the infamous cigarette counterfeiting centre in Guangzhou, each of the 3,000 counterfeit cigarette traders was required to pay a ‘protection fee’ of 500 Yuan (approximately £ 45) per month to

extortionists as a compulsory charge for their ‘protection’ services. Violence was often used to enforce the payments.

### *Discussion*

The counterfeit cigarette business highlights “the enormous symbolic presence that images of organised crime have in popular discourse” (Sheptycki, 2008: 23). Our study suggests that, unlike popular representations, cigarette counterfeiting in China, just as with illegal tobacco-related activities in other contexts, is characterised by a high degree of heterogeneity and a range of organising the business (see van Duyne, 2003; von Lampe, 2003; 2005; Antonopoulos, 2008). There appear to be independent ‘entities’ involved in different parts of the business and actors who are subcontracted to provide commodities and services about the process.

There is a relatively high level of sophistication in the business, not so much however, in relation to the links between actors or stages of the business but more in relation to the technical sophistication necessary for the production of counterfeit cigarettes. Relationships between actors in the business are very often based on a customer-supplier relationship or a ‘business-to-business market’, which is a very common characteristic of the Chinese (legal and illegal) economy (see Simons, 2009).

A large number of individuals are involved in illegal tobacco-related activities simply because this offers them an entrepreneurial opportunity in a relatively low-risk environment, and in the absence of state welfare provisions that address the income inequalities and economic exclusion facing, particularly, internal migrants (see Wing Lo and Jiang, 2006).

The role of corruption and violence in the cigarette counterfeiting business is not to be underestimated. Corruption, although not mentioned in all counterfeiting cases we encountered, seems to be at least a facilitating factor of a large part of the business. In addition, although violence could attract the unnecessary attention of law enforcement, it is nevertheless more prevalent in the counterfeit cigarette market in China than in other contexts. This perhaps highlights the fact that the American and European experience of illegal markets may not be entirely compatible with the extremely diverse Chinese context. It also highlights the dynamism of illegal markets in this particular country, and calls for additional, preferably empirical research in this ‘exemplary society’ (Bakken, 2000).

We mentioned earlier that the illegal cigarette business in general and counterfeiting in particular emerged as a problem in China in the late 1970s and early 1980s when the ‘open door’ policy and economic reform made profit and economic development a national movement (*quanming jingshang*) (Liu, 2005: 619). The economic reform facilitated the emergence of cigarette counterfeiting in a variety of ways. Firstly, there was the paradox of the private sector becoming increasingly dynamic while at the same time the tobacco industry continued to remain a state monopoly. It proved extremely difficult for private entrepreneurs to become involved in the huge and highly lucrative Chinese market, and the smuggling and counterfeiting of cigarettes provided the only alternative avenues to market entry.

Secondly, the transition to a market economy and the subsequent restructuring of the tobacco industry led to the *technical* facilitation of the cigarette counterfeit business by setting free two important types of resources: skilled workers and production machinery. Simultaneously, the reluctance of licensed cigarette sellers to trade in cheap legal cigarettes due to the small profit margin and the subsequent reduction or even cessation of production of cheap cigarettes by local authorised factories, despite the demand for cheap cigarettes, created a niche in the market that was filled by counterfeiters. It seems that in the case of counterfeit cigarettes, authorised manufacturers and the state have been ‘victims’ of their profit-oriented mentality. Thirdly, the trade liberalisation which has been an important pillar

of the economic reforms not only allowed for an increased volume of legitimate trade but also created a façade for illegitimate trade (Andreas, 1999), of which counterfeit cigarettes are an important aspect.

However, it is not only the opening of the Chinese market and economy to the rest of the world that has facilitated the booming of the cigarette counterfeiting business; it is also the other way around. The most populated country of the world has an annual development rate of approximately 10%, which is four times higher than the average development rate of developed world economies. This development is ‘fed’ to a great extent by the country’s cheap labour, which along with the governmentally maintained low exchange rate for the Chinese currency, directly or indirectly support the export of Chinese products. Counterfeit cigarettes, like other licit and illicit commodities, fall within the category of cheap exported goods. However, counterfeit cigarettes are also an indication of the importance of tobacco for China and the commodity’s surplus. The counterfeit cigarette business has informalised the process of manufacturing cigarettes to an extent that a comparative advantage has been created for unauthorised manufacturers over authorised Chinese and international manufacturers (see Castells and Portes, 1989).

The way in which the *legal* and the *illegal* intersect is also evident in the Chinese counterfeit cigarette business. Cigarette counterfeiters benefit from the legal sector and some legal businesses also benefit from cigarette counterfeiters in various ways. The case of the air-companies mentioned earlier is just one striking example of this symbiosis.

When it comes to the links between China as the counterfeit cigarette *source* country and (primarily) western markets, the role of the western states as the ultimate “market determiners” (van Duyne, 2007) by imposing prohibitive taxes on cigarettes, a socially and culturally-embedded commodity, has to be highlighted. High taxation imposed by governments has contributed to an environment of demand for cheap cigarettes, which has been exploited by entrepreneurs capitalising on huge price differentials and “global market ambiguities” (Hornsby and Hobbs, 2007: 565). Overall, cigarette counterfeiting in China, and by extension the rest of the world, appears to be an integral part of the neo-liberal marketplace jigsaw in the country (and beyond), and a result of an uneasy symbiosis between state planning, local government competition emphasising profit, personal greed, aspirations and needs, as well as market dynamics that are exacerbated by the forces of globalisation.

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