The Gazette

Tobacco insider talks: Major firms were deeply involved in cross-border smuggling, former executive says

By *WILLIAM MARSDEN*. **The Gazette**. Montreal, Que.: Dec 18, 1999. pg. A.1

Feb. 24, 1999, was not a banner day for Les Thompson. Arrested by U.S. Customs agents in the Ontario city of Windsor, cuffed and thrown into jail, the RJR-Macdonald sales executive suddenly became the slick, hard-driving, unscrupulous face of big tobacco.

U.S. prosecutors claimed they had nabbed the man behind a billion- dollar tobacco-smuggling network that in the early 1990s pumped billions of black-market cigarettes through the Akwesasne Indian reserve at Cornwall and into Canada.

Alone in a concrete lockup, Thompson recalled the words of a company lawyer nine months earlier, words spoken just after he had learned he was a target of a police investigation: "Stand tall through this, Les. We will stand behind you. We don't need wobbly legs here. The government is sabre-rattling. This thing is going to go away."

Eight days after his arrest, a company-paid lawyer finally showed up at his jail cell in Syracuse, N.Y.

"I've got good news and I've got bad news," the lawyer said. "The good news is I'm here. The bad news is the company will not support a trial."

The company Thompson had served for so many years, topping its sales charts, had turned on him.

Steven Goldstone, CEO of parent company RJR Nabisco, intimated to shareholders that Thompson was a rogue who had redirected Europe- bound cigarettes back into Canada without the top brass knowing about it.

"Employees are prohibited from engaging in smuggling or other violations of the law," he said, adding that there will always be "the risk that dishonest employees ... will find ways to circumvent controls for their own personal benefit."

A month later, Thompson pleaded guilty to laundering $72 million U.S. from smuggling tobacco into Canada and agreed to a seven-year sentence. A federal judge in Binghamton, N.Y., will confirm the sentence Monday.

Thompson was the only RJR executive to be charged in connection with cigarette smuggling. The company continues to deny it played any role in encouraging it.

But an investigation by The Gazette, which includes an exclusive interview with Les Thompson, shows that RJR-Macdonald carried out a campaign to funnel billions of cigarettes through a handful of traders and flood the marketplace with the black-market tobacco.

The strategy was planned and executed by senior executives, with the knowledge and approval of their parent companies, RJR International in Geneva and RJR Nabisco in New York City, according to documents obtained by The Gazette.

For years, Canada's three big tobacco companies have denied allegations they encouraged or condoned smuggling operations that moved more than 28 billion cigarettes into the black market from 1990 to 1994, when Canadian tobacco taxes were at their highest. The companies have claimed they simply sold to licensed traders who regularly ordered their products. What happened to the cigarettes, they have said, was not their concern.

The Gazette investigation reveals, however, that big tobacco companies solicited the business and fought to hold onto it.

It reveals for the first time the inner workings of big tobacco in the international smuggling game and how the industry marshaled its forces to make huge profits out of a black-market economy that defrauded Canadian taxpayers of an estimated $5 billion in tobacco taxes.

Each of Canada's big three tobacco companies - RJR-Macdonald, Rothmans Benson & Hedges Inc., and Imperial Tobacco - organized their own corporate structures or signed special contracts to service this black market. They did so with an eye specifically on the tiny Akwesasne Indian Reserve at Cornwall, which straddles the Canada-U.S. border and was the funnel through which the vast majority of cigarettes were smuggled back into Canada.

Les Thompson, the investigation shows, was little more than a frontline soldier in the massive corporate effort by RJR-Macdonald to use the smuggling networks to make vast profits, increase its market share and ultimately pressure Canadian governments to reduce tobacco taxes.

Far from simply selling cigarettes and fine-cut tobacco to licensed dealers, RJR executives partied with smugglers, exchanged expensive gifts, pressured traders to buy more cigarettes and then joked about the huge profits they were making from the "feathers." Employees were cautioned to be careful what they wrote on paper and were told to keep their mouths shut because "loose lips sink ships."

"The company is chasing this business," Thompson said of RJR- Macdonald (now called JPI-Macdonald after being sold to a Japanese company). "Let's be very clear. The company didn't say, `Hey, Les, good move, bringing in a container a week. Where did that business come from?' They solicited the business. They secured the business, and they chased the business and exploited the business. Let's be very clear on that. It wasn't extra business. It became the business."

Into the Black Hole

Smuggling in Akwesasne took off in 1988 when Ottawa and the provinces, in a move to discourage smoking, imposed major tax increases on tobacco. By 1991, the price of a carton in most provinces had risen to more than $45 and the market for tax-free tobacco exploded.

Rothmans Benson & Hedges were the first Canadian brands on the black-market scene. Imperial and RJR-Macdonald followed. Before long, the thin strip of land on the American side of Akwesasne sported six large warehouses continuously stacked to the roof with cases of Canadian-brand cigarettes waiting to be smuggled across the St. Lawrence River, which conveniently narrows as it flows past the reserve. From there, the tobacco moved easily into the Canadian black market. Akwesasne was a smuggler's dream.

While all three major Canadian tobacco companies set up or used existing corporate structures to feed the black market, RJR- Macdonald was probably the most aggressive, clumsy and blatant.

Yet it was also the last to get into the market. In 1991, top executives at RJR-Macdonald's 60th-floor head office at First Canadian Place in downtown Toronto worried over field reports that the more aggressive U.S. marketing by both Rothmans Benson & Hedges and Imperial was eroding profits and market share on their Export `A' cigarettes. Essentially a single-product company with a declining blue-collar brand, RJR-Macdonald felt it could not stand by and watch this happen.

An RJR-Macdonald marketing and planning study dated May 6, 1991, and entitled "Canadian Brands in the U.S. - the Border Store Opportunity," notes that the company's share of the market was so low, it had to take "drastic and immediate action to obtain our fair share or better."

So in 1991, RJR-Macdonald decided to invest $1.7 million in "blitzing" this market with 12 sales representatives controlled by mid-level executives Les Thompson and Nigel Holmes. The sales reps would cover every major border area from New Brunswick to British Columbia "missionary selling" - venturing into virgin territory - to major stores near the border. The goal was to increase market share to 25 per cent of cross-border trade.

But the plan was a bust. The black market grew so large in Canada that Canadians didn't have to cross the border for cheap tobacco.

By the end of 1991, company executives realized that their sales efforts in border stores were not paying off. So, Thompson said, they "took the gloves off and went directly into the black market."

"Imperial and Rothmans were very, very successful in the business," he said. "You could see their volume growing almost weekly. It was from the company's standpoint a pretty frustrating period of time. We just obviously hadn't met the right people."

That problem was about to be solved.

Three men - Larry Miller from Las Vegas and two brothers, Lewis and Robert Tavano from Niagara Falls, N.Y. - wanted to expand their small but growing business of supplying cigarettes to Indian smugglers.

The Tavanos were well-known, politically connected figures in Niagara Falls. Robert had been a prominent Republican Party chairman until he was convicted in 1975 of defrauding a local county government of $384,601 U.S. and of bribing two local politicians. His brother Lewis was charged but not convicted in the 1970s of participation in an illegal gambling ring. He later moved to Las Vegas, where he ran a sports bookmaking and loan operation. Buffalo police had linked the brothers to the late Stefano Magaddino, a Buffalo crime boss.

Larry Miller was a Las Vegas casino equipment salesman who had come to the Akwesasne reserve in 1989 to sell slot machines. He gave up that business when he saw the big-profit opportunities in cigarette and liquor smuggling.

Through his Las Vegas connections, he joined up with the Tavanos and formed LBL Trading Inc. (for Lewis, Bob and Larry), based in a small house along the main strip in downtown Niagara Falls, N.Y.

They obtained a U.S. federal licence to sell tobacco to Indians and, with money initially fronted by Las Vegas investors, began by purchasing Rothmans Benson & Hedges brands out of a free-trade warehouse in Buffalo owned by Tim and John Palisano. (Free-trade warehouse owners are essentially freight-forwarders, storing cargo until it is picked up.)

The Palisanos' warehouse was stacked to the roof with Rothmans products which LBL and other companies trucked to Akwesasne.

LBL was a small player in this business and began looking for a more direct line to the tobacco manufacturers. Again the LBL owners relied on their Las Vegas connections.

Through an executive with the Las Vegas Four Seasons Hotel, they obtained an introduction to a senior executive at RJR-Macdonald.

The introduction was timely. According to a company source, RJR- Macdonald's duty-free section had been unsuccessfully trying to push various ship chandlers (who supply duty-free goods to ships leaving for international waters) and duty-free companies in Montreal, Toronto and Vancouver to buy containers of cigarettes which they would divert to the U.S. to supply the smugglers. Some of these companies had set up affiliates in the U.S. officially to receive these shipments and then send them back through Akwesasne.

Yet despite constant sales pressure, these customers never bought enough volume to satisfy RJR-Macdonald's demands.

"We had them in Toronto a number of times," Thompson said. "Sat down with (sales vice-president) Stan Smith and myself. They were frustrating times, because these people were so slow to fill in the volume request that we were putting on them."

Then LBL showed up. Thompson said he was directed in March 1992 by Smith, his boss, to "call Bob Tavano and specifically set up a meeting."

"I asked Stan who Bob Tavano was and Stan Smith told me that (RJR- Macdonald CEO) Ed Lang had been introduced to the Tavanos ... that Ed Lang had received a call from an executive at the Four Seasons, a mutual friend, and he in fact handled the introduction to Lang to the Tavanos."

Thompson and his assistant, Wade Blonheim, met with Miller and the Tavanos in March 1992 at the Como Restaurant, a popular Italian restaurant and deli in downtown Niagara Falls, N.Y. Thompson said they showed him their trading licence which allows them to sell to Indian reserves and boasted they had been successful with Rothmans brands but felt they could do more volume if they had a direct supply of Export `A's from RJR.

"These people were ready to do business," Thompson said. "We weren't doing very much business there (across the border) and we were in the process of shifting gears and going direct to the black hole."

The Tavanos were prepared to start with one container a week and possibly more later.

When Thompson got back from the meeting, he said, he gave a copy of LBL's Indian trading licence to Paul Neumann, RJR-Macdonald's vice-president of finance, whose department would vet the company's application to become a direct buyer.

Approval was almost immediate. A process that usually took weeks was fast-tracked. No applications had to be filled out or financial statements presented. Within a few days, LBL was granted a direct line to RJR-Macdonald. All it had to do was pay up front for every shipment. The word on LBL right from the beginning was a go. Basically, send in the money and we'll ship the goods.

Checking for Bugs

Les Thompson, now 52, was a hard-driving RJR-Macdonald salesman who had worked his way up the ranks by always reaching or exceeding his sales projections. An exceptionally fit long-distance runner, he was considered by colleagues to be aggressive, loyal, though not always likeable. But he brought in the deals and relentlessly pushed customers to buy more. He had been Ontario sales director and now Smith charged him with the task of pushing tobacco on LBL and a string of other third-party distributors the company had lined up.

Les Thompson never asked why. He just asked how high. But blindly accepting this job was probably the biggest mistake he would ever make. RJR's approach was "take no prisoners," and Thompson was the field general who would end up behind bars.

Shipments began almost immediately. Every delivery was prepaid. "They would fly cheques into whatever, Toronto Island, to our office, plenty of times couriers driving right to our office. Nothing would be shipped until it was paid," Thompson said.

"We were shipping one container a week, which represented 10 million cigarettes or about 20 per cent of our weekly production."

Within a short time, RJR was shipping three to four containers a week to LBL and other distributors. Sales briefs to Smith demonstrated that what the company called the "parallel market" or "re-entry market" was fast becoming first 30, then 50 per cent of the company's volume on a weekly basis, all going through the black hole of Akwesasne.

The cigarettes were sent to a Palisano free-trade zone in Buffalo where they were picked up by LBL and five other traders who shipped directly to Akwesasne.

So fast and furious was the business that RJR-Macdonald had no time to change the packaging to meet export requirements. So Palisano had to hire people to unwrap every carton and place a "Not for Sale in Canada" sticker on each package, then rewrap them for delivery to Akwesasne to make the shipments look legitimate, Thompson said.

There was "no doubt in anybody's mind at any level of management at First Canadian Place where these people were going to be selling cigarettes," Thompson said.

With more than 50 per cent of its volume directed to the "parallel market," RJR-Macdonald became concerned about the legal implications, and decided to consult its outside counsel, Tass Grivakes of the Montreal law firm Mackenzie Gervais.

Thompson said he and Smith were told by Grivakes the company was entering into a gray area that, while not illegal, could be a political hot potato.

Thompson commented: "You say, `Gee, Les, you sound like a pretty naive cat here. You didn't even know that this was illegal.' I had been coached prior to getting involved in this business by a company lawyer. They convinced me that this is a gray area in the business. It's not black. What you're doing is a loophole in the business. `Go forward, young man,' that type of thing. It wasn't like, `Jeez, Les, you better be very careful out there. You could get arrested for managing this type of business.' That was never suggested."

He said the company also hired some retired RCMP officers to check all their offices and the homes of executives for bugs. None were found.

Nevertheless, concerned about dealing directly with smugglers, RJR-Macdonald decided it needed to distance itself further from LBL and its other border distributors.

So in mid-1992, RJR-Macdonald set up a company in Winston-Salem, N.C., called Northern Brands International Inc. and registered it in Delaware with U.S. directors.

It was a subsidiary of RJR Nabisco Inc., an astonishing decision since it linked the smuggling directly to the U.S. parent company while distancing it from RJR-Macdonald.

RJR-Macdonald also opened a second front. In mid-1992, ostensibly to avoid a threatened federal export tax on tobacco, RJR-Macdonald moved cigarette-manufacturing machines out of its Montreal plant to Puerto Rico, where the company began manufacturing Export `A's for shipment to tax-free zones in Buffalo and New Jersey and then into Akwesasne.

To disguise the shipments, R.J. Reynolds Tobacco International Special Markets in Winston-Salem, which at the time was run by a Canadian named Franco Gabriele, signed a deal in March 1992 with International Duty-Free Trading N.V. (IDF) and its managing partner Bryan Harms, a shipping agent based in Aruba (formerly the Dutch West Indies).

According to an IDF letter outlining the deal and obtained by The Gazette, IDF agreed to act as a broker and shipper for "Canadian brands to some of RJR's accounts in the U.S. that serviced accounts operating on the Indian reservations straddling the Canadian-U.S. border."

IDF would handle not only this freight forwarding, but also all money transactions, accounts receivable and payable. The cigarettes would be shipped via Sealand Shipping Line to IDF in Aruba. The company then reshipped them to Elizabeth, N.J.

According to a letter sent in 1994 to RJR-Macdonald by Harms, IDF's accounting was simply book entries. IDF never actually handled any money. That was controlled by RJR-Macdonald. Nor did IDF ever contact any of the buyers. That too was handled strictly by RJR- Macdonald. On the books, however, RJR-Macdonald was another step removed.

By the end of 1992, IDF saw more than $30-million U.S. worth of cigarettes going through its books. But, according to the letter, not one penny went into an IDF account. It was all paid by LBL and other distributors directly to RJR-Macdonald's headquarters or through bank accounts in Puerto Rico or North Carolina.

(In 1993, RJR-Macdonald would put another $35.7 million U.S. through IDF's books. In 1994, Harms threatened to sue the company. In a letter dated Feb. 22, 1994, to Ed Lang and labeled "Confidential," IDF claimed it was owed more than $3 million U.S. for services rendered. The letter outlines the entire Aruba operation. RJR-Macdonald promptly paid Harms the money owed, Thompson said. In an interview, Harms refused comment claiming he needed permission from U.S. prosecutors in Syracuse to speak about his dealings with RJR-Macdonald.)

At this point, RJR-Macdonald was now supplying smugglers from plants in both Montreal and Puerto Rico.

It also established a third sourcing plant. In 1992, it contracted with Standard Commercial Manufacturing in Wilson, North Carolina, to produce Export `A' fine-cut tobacco - loose tobacco sold in a can. Every leaf of this tobacco would be targeted for the black market, Thompson said.

By 1993, Thompson said, all three plants were working overtime supplying distributors for the Canadian black market. The "parallel market" business grew to almost 60 per cent of RJR-Macdonald's net profits. Smuggling was fast becoming the company's main source of income and the principal reason why its Canadian market share was increasing.

The growing sales energized a company that for years had watched helplessly as the popularity of its main brand, Export `A', declined. The increased volume and profits meant bigger bonuses for everybody. Just before Christmas in 1992, RJR-Macdonald persuaded LBL to ante up $5 million U.S. to pay for shipments that wouldn't be delivered until 1993 just so the higher-ups could enter them into the 1992 books and claim bigger bonuses.

But LBL couldn't get the cheque to Toronto because of a snowstorm. So Thompson said he flew to Dorval airport where he picked up LBL's cheque from a courier sent by Miller. Then he dashed to the nearest Royal Bank branch which had been kept open just so the money could be deposited into RJR-Macdonald's account before the company closed its year-end books.

When he arrived back in Toronto, fellow executives called him "partner" and gave high fives. "Pal, you just solidified your career to retirement," one told him.

Executives were ecstatic about the new business. Thompson recalls them making Indian war cries when he passed them in the executive corridors. "Wooo, wooo, wooo!" They backslapped him and addressed him as "Chief."

Once, when TV news showed seizures of competitors' cigarettes, he said Smith told him: "Either you are not selling enough or your customers are doing a better job than the competition's in avoiding seizures."

Still, there was a growing desire to distance the company from the sales to smugglers. The need to consolidate and create a tightly controlled corporate structure became clear to top RJR-Macdonald executives and to the company's parent, RJ Reynolds Tobacco International, which at the time was based in Winston-Salem. (It would move the following year to Geneva, Switzerland.)

RJR Tobacco International organized a meeting of top financial people at the Graylyn Conference Centre in Winston-Salem on March 5, 1993.

Representing RJR-Macdonald was Peter MacGregor, an executive in the company's finance department and soon to become general manager of NBI. MacGregor made his presentation at about 10:15 a.m. It lasted about 30 minutes and outlined the reasons why and how RJR- Macdonald would use NBI as its conduit for selling cigarettes to the smugglers.

He described the high taxation problem in Canada and the "strong demand for tobacco products in lower-(tax) or tax-free jurisdictions" - that is, Akwesasne.

It was decided that all product from the Montreal plant destined for the United States would be sold to NBI, which in turn would handle all warehousing in free-trade zones and all sales to third- party distributors such as LBL.

While NBI would be owned by RJR Nabisco, it would take all its instructions from RJR-Macdonald. Its payroll would be met by RJR Tobacco International.

MacGregor's presentation noted that this new structure would assure that a dedicated sales team was in place to push as many cigarettes as possible in the northern New York area.

RJR-Macdonald relocated Les Thompson and Peter MacGregor to Winston-Salem - Thompson as sales director and MacGregor as finance director and general manager. Essentially, they were in charge of pushing as much product on the smugglers as possible. NBI, with its two employees and a secretary, was basically an American sales tool for RJR-Macdonald.

"(It was) of a highly sensitive nature, and the consideration for moving to the States was that it was very sensitive here, an out-of- sight out-of-mind type of an application of business," Thompson said.

Before he left for Winston-Salem in February 1993, RJR-Macdonald threw Thompson a going-away party. It was held at an Italian restaurant in Oakville, west of Toronto, and was hosted by Stan Smith who lived close by in a large clapboard home on the lakeshore.

The party went on into the early hours of the morning with about 60 to 70 raucous guests plus their wives or girlfriends. At its peak, Smith presented various gifts to Thompson and his wife.

"Les, we've got a special gift for you and it took my secretary two days to find," he announced. "When you open the gift all I ask is that you put it on and you wear it. You have to wear the gift."

Thompson opened the box and pulled out a large Indian headdress. When he put it on, its dangling eagle feathers almost touched the floor. Partygoers laughed and cheered.

"The message was clear: `Les was going to be selling lots of cigarettes to the Indians,' " Thompson said.

Ensconced in NBI's offices at RJR Nabisco in Winston-Salem, Thompson began working the tobacco traders as he had done at head office in Toronto. Documents obtained by The Gazette show that weekly, sometimes daily, reports were sent by NBI to RJR-Macdonald seeking permission on each sale. Stan Smith signed off on them.

Thompson said RJR International lawyer Pierre Bourassa made regular visits to NBI offices and received regular briefings from Thompson and MacGregor on the progress of the business.

NBI regularly sent salesmen into Akwesasne to check inventories of RJR-Macdonald and its competitors in Indian warehouses, and assess RJR-Macdonald's market share. Both MacGregor and Thompson went along on some of these field trips. Thompson said he made about eight trips to Akwesasne where he and other employees inspected warehouses and talked to Indian smugglers. All reports were sent to head office, he said.

One sales report dated Sept. 16, 1993, and written by Chris Fragomeni, an RJR-Macdonald salesman, referred to the Indian warehousing operations as "gray-market accounts." It stated that RJR- Macdonald products accounted for between 40 and 60 per cent of inventories in the reserve's six warehouses. Imperial had 15 to 40 per cent and Rothmans Benson & Hedges 10 to 20 per cent. It was clear NBI was making headway. RJR-Macdonald executives began referring to it as "Nothing But Income."

Competition to supply the "parallel" or "re-entry" market was expanding and by 1993 each of the three major Canadian tobacco companies were using basically identical corporate structures all feeding the same distributors who in turn fed the same Indian smugglers at Akwesasne.

Imperial Tobacco had decided in 1992 to go full steam ahead in supplying what it called its U.S. customers. First, however, the company had to settle longstanding trademark and royalty issues.

Since the Philip Morris company held the rights to sell Players in the U.S., Imperial signed a contract on Sept. 29,1992, with Philip Morris to sell Players to the U.S. company. The confidential agreement, obtained by The Gazette, specified that the Canadian taste, quality and packaging would be maintained and each package would carry the legend "Made in Canada by Imperial Tobacco, Montreal, Canada for Philip Morris Inc."

Documents obtained by The Gazette show Philip Morris's first order was for 150 million cigarettes or 15 40-foot containers. The first shipments were made Nov. 23 directly to Philip Morris.

Philip Morris sent most of the loads to a New Jersey ship chandler named J. Stanley Inc., who then sold them to LBL and other distributors.

Imperial marketed its du Maurier brands through a Miami-based trader named Jorge Azel and his company SMT. Most of the SMT du Mauriers were trucked to warehouses in Port Elizabeth, New Jersey, and then sold to third-party distributors such as LBL or Milhem Jr. Attea, a Buffalo trader, sources said.

Because of trademark restrictions, Imperial was not allowed to sell du Maurier into the U.S. without paying a 5-per-cent royalty to Peter Jackson (Overseas) Ltd., which, like Imperial, is owned by British American Tobacco (BAT). Since the vast majority of du Mauriers sent south were smuggled back into Canada, Imperial wanted a new deal. So in June 1993, Imperial's president, Don Brown, negotiated a royalty reduction to 2 per cent.

In a letter to BAT executive Ulrich Merter in London, England, Brown wrote: "Until the smuggling issue is resolved, an increasing volume of our domestic sales in Canada will be exported, then smuggled back for sale here."

In 1993, Imperial sent more than 6 billion cigarettes, or at least 600 40-foot containers, into the U.S., according to figures the company gave The Gazette.

One smuggling source told The Gazette that Imperial actively solicited business from smugglers. He said he met with an Imperial marketing agent named Richard Ward in the executive offices of the company's Montreal headquarters on at least three occasions in 1991 where they discussed purchasing tobacco which the company would deliver to the U.S. for the smugglers to bring back into Canada.

"It was clearly identified that the goods would be in the Canadian black market," he said. "Richard Ward suggested that he would deliver cigarettes to a free-trade zone in Miami or any other free-trade zone as long as it wasn't too close to Akwesasne." He added that the company didn't want to appear to be feeding the black market.

Rothmans Benson & Hedges was a similar story. Its equivalent of NBI was an already established affiliate called Tobacco Exports International, run out of Atlanta, Ga. Its cigarettes went to the same smuggling networks. In 1992, it sent 3.5 billion cigarettes into the States. Most of them were smuggled back into Canada.

Sources said Imperial and Rothmans used a relabelling plant set up in Champlain, N.Y., and run by a Montrealer named Michel Sylvestre. The plant was used to put American Surgeon-General stickers on the packages and reseal them with cellophane to meet U.S. packaging requirements and also so they wouldn't look as though they were ultimately destined for Canada. One source said Imperial helped obtain the machinery for this operation from England.

With all three major cigarette manufacturers now deeply involved in feeding the black market, the chase was on to secure the loyalty of their third-party distributors, like Miller and the Tavanos.

An essential part of the marketing and sales strategy became entertainment. RJR-Macdonald approved about $1.6 million U.S. for NBI to entertain customers, Thompson said. "Whatever they wanted was not out of the question."

This meant fishing and gambling trips to the Bahamas and to Sonora Lodge, a class `A' fishing and leisure camp in British Columbia. The Tavanos and Larry Miller and his family were invited to golf tournaments, Formula One racing, and hockey and baseball games where they received VIP treatment. They schmoozed with RJR- Macdonald CEO Lang and other senior executives. The Tavanos gave gifts to RJR-Macdonald employees which included free weekend trips to Las Vegas; Thompson received a 1994 Cadillac from Miller.

NBI also dealt heavily with SMT. Its owner, Jorge Azel, loved baseball. So Lang flew him up for Blue Jays World Series games.

In return, the customers continued to buy container loads of Export `A', stacking warehouses south of the border to the roof.

Throughout 1993, NBI's business boomed. That year it sold 5 billion cigarettes -including fine-cut - into the black hole, Thompson said. Essentially a two-man shop in Winston-Salem, it nevertheless accounted for 63 per cent of RJR-Macdonald's net profit.

By the end of 1993, NBI profit reached $78 million U.S. The company's total 1993 net profit was $122 million U.S.

Before the company began dealing directly into the black market, RJR-Macdonald's total net earnings were about $74 million U.S., Thompson said.

What's more, its aggressive sales policy had pushed its share of the Canadian market to about 20 per cent. Even though the cigarettes were sold in the U.S., the sales were entered into the company books as Canadian domestic market share.

"So when the CEO stands up in front of his boss, he can say:

`Well, you know, we made $122 million, we sold 8 billion units and we drove our market share in Canada to over 20 per cent through these efforts,' " Thompson said.

`Nothing but Inmates'

Statistics Canada figures show the big three tobacco companies exported 14.2 billion cigarettes into the U.S. in 1993, plus about 3 billion units of fine-cut tobacco. This does not include the cigarettes manufactured in Puerto Rico or the fine-cut made in Wilson, N.C.

The heady pace at which the tobacco companies were feeding the black hole of Akwesasne finally forced the federal and provincial governments to roll back taxes in February 1994 by as much as $20 a carton. Exports to the U.S. plummeted to about 2 billion cigarettes and 600 million units of fine-cut.

But the smuggling did not entirely dry up. Even with the thinner margins, some traders found it profitable. RJR-Macdonald continued to ship cigarettes through NBI to third-party distributors such as the Tavanos and Miller. NBI's net profits nose-dived to below $10 million U.S. But with only two people on the payroll it was still considered a win-win situation. NBI was a sort of insurance policy against future Canadian tax hikes, Thompson said.

Only the four western provinces kept their taxes high. So Thompson said Stan Smith told him to "get your ass up to Alaska" and evaluate whether cigarettes could be sold to smugglers through free- trade zones in that state. Thompson reported back that the geography was too much of an impediment.

NBI first learned there might be a police investigation into smuggling-related offences in January 1994 when it received a subpoena from a U.S. district court in Buffalo, N.Y. A grand jury wanted to see documents relating to shipments of cigarettes into a Buffalo free-trade zone.

By 1995, the investigation was in the hands of U.S. Assistant District Attorney Gregg West, head of the district's permanent strike force. He targeted Miller, his family, the Tavanos and their main Indian customers.

He also targeted NBI and Les Thompson. Because he was RJR- Macdonald's front man, Thompson's name seemed to be on every smuggler's lips.

When police told Thompson in June 1998 that he was the focus of a smuggling investigation, RJR-Macdonald executives joked that NBI now stood for "Nothing But Inmates."

Thompson said he was constantly told to "stand tall" and keep his mouth shut. He said company officials were worried that MacGregor, NBI's general manager, might be talking to police.

At a skins golf match in August 1997 in Whistler, B.C., Thompson said: "Ed Lang took me aside and said: `I want you to go back and tell MacGregor, `Loose lips sink ships.' "

During this time, Thompson was still working out of Winston- Salem directing duty-free sales in the northeast U.S. He said the company regularly supplied ship chandlers with containers of tax- free Winstons to be sold in the high tax markets in Europe.

When European police began seizing these shipments, Thompson said he was told to cut back on the sales to these chandlers to one load a month. They wanted to keep the distribution channels alive, he said.

He said he was then shifted to Miami where he would operate the duty-free sales along the Mexico border. "That largely is a cross- border environment very similar to what went on in the black hole in Cornwall," he said.

Meanwhile, RJR-Macdonald officials had begun leaving the company. Lang had resigned in 1993, retiring to a condo in Naples, Fla., though he remained on the board of directors. Peter MacGregor left NBI and took a job with Porsche America in Atlanta, Georgia.

Paul Neumann, Roland Kostantos, both vice-presidents of finance at RJR-Macdonald, and Pierre Brunelle, company president in charge of the Montreal plant, moved to Geneva to work for RJR International.

Stan Smith, who became chief operations officer, took a severance buyout in 1998. Last September, he moved to London, England.

Les Thompson was the only tobacco executive to be charged.

As for the firm he helped run, Northern Brands International Inc. pleaded guilty to a minor customs infraction and paid $15 million U.S. in fines and forfeiture. As part of the agreement, the U.S. Justice Department Northern District pledged not to take any further action against RJR Nabisco, the New York parent company.

In November 1998, Philip Morris reported to shareholders that it is under investigation in the U.S. for alleged involvement in tobacco smuggling into Canada.

Meanwhile, the RCMP have launched three task forces to probe industry complicity in the smuggling. The Mounties raided RJR- Macdonald's head office in May. The firm has stated it is co- operating with the investigation and beyond that cannot comment.

A Cornwall-based RCMP task force is targeting U.S. distributors and last spring charged the J. Stanley company and its owners with conspiracy to defraud the Canadian government.

A Montreal task force is investigating Imperial Tobacco.

The federal justice department is also assembling proof for a possible billion-dollar lawsuit against the industry for tax fraud. The government is planning to launch the suit in New York State.

This year, RJR-Macdonald offered to settle for $100 million. The government rejected the offer.