

Committee: Economic and Social Council

Issue: Minimizing shadow economy leakages

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INTRODUCTION

The shadow economy, or black market, is a much larger part of the worldwide economy than most people realise. The illegal trade, which ranges from weapons to counterfeit clothing and electronics, is currently estimated to be worth approximately \$10 trillion, and employ almost 1.8 billion people, i.e. almost half the world's workers, with no signs of either figure decreasing.

The size of the black market makes it a large problem for the legitimate part of the economy. Any profits for the black market represent either losses for legitimate businesses, and hence the government that taxes them, or the sale of illegal and dangerous goods such as weapons or hard drugs. It is, therefore, imperative that the black market is contained and eventually eliminated, to prevent it from causing any more problems.

There is no single 'silver bullet' solution that can achieve that goal. Each segment of the black market is different from the other, meaning that a solution that could eliminate illicit arms trade would be completely ineffective on the illegal trade of drugs. Still, there is a large number of solutions that have been applied - with varying degrees of success - to combat the black market, perhaps most notably the legalization of marijuana that has been gaining traction in the latest years.

DEFINITION OF KEY TERMS

Shadow Economy

Also known as the black market, the term refers to a market which does not conform to the legal framework of the state. The shadow economy is usually distinguished from the gray or unreported economy, which refers to any non-declared transaction; this is often done to evade taxes while trading legal goods and services.

Counterfeit Goods

Products made to resemble those of another company, without that company's authorization. These products are usually of inferior quality to those of the original brand.

Legalization/Decriminalization

The two terms are often used interchangeably when referring to the changing of the legal status of a good or service. Decriminalization refers to loosening the penalties for possession, removing any imprisonment penalties or lasting criminal record, while keeping the supply side of drug trade illegal. Legalization, on the other hand, means that the whole supply chain becomes legal, and that there are absolutely no penalties for possession, sale or cultivation (in the case of narcotic substances). Notable cases are those of marijuana and prostitution, which have been legalised in certain European countries.

War on Drugs

A term coined by US president Richard Nixon in 1971 to describe his policy of strong regulation and persecution of drugs, as well as the incarceration of their users. The policy has continued to this day and is currently being strongly criticised as it is costly and demands great manpower.

BACKGROUND INFORMATION

Drugs

Illegal drug trade is the largest illicit business in the world, estimated to be worth close to \$300 billion². Drug trade is a worldwide phenomenon, with very few countries exempt. There has been a variety of different methods in an attempt at reducing drug trade, including the legalization or decriminalization of some (or even all) narcotics, which have been put into effect in various countries, most notably Portugal, which 14 years ago chose to decriminalize the possession of all drugs, from marijuana to even heroin³ (see Legalization/Decriminalization under Previous Attempts to Solve the Issue).

One of the reasons for the large amount of money spent on drug trade is due to transport. Because of strong border controls, the mark-up of the price of drugs due to transport is increasingly affecting their final price. For example, "Tea is [...] cheaper than marijuana, even though the latter is easier to cultivate. Quality weed sells in the US for \$300 to \$450 per ounce [...]. Even the fanciest teas go for much less. India's most expensive tea ever made runs about \$1,850 per kilo (about \$53 per ounce)." ⁵ On the contrary, "shipping one kilogram of cocaine using FedEx would cost between \$55 and \$115, depending on the location." ⁵.

Weapons

Illicit arms trade is considered as the one of the most harmful sectors of the black market, as it allows for the continuation of various conflicts throughout the world, and causing 300,000 to half a million civilian deaths per year. It is also one of the most profitable, estimated to be generating over

\$1 billion per year. Weapons trade can be split in two categories; "small arms" and "light weapons". Namely "small arms and light weapons" refers to weapons made for non-army use and light arms are military grade equipment. Aside from enabling the conflicts in which they are first used, illicit arms and weapons usually remain active for a long time after their use was banned, or the conflict in which they were originally used in ended, and hence preventing the stabilization of the region. This leads to the economic impact of illegal weapons, in that they prevent less economically developed countries (referred to as LEDCs) from reaching their full economic potential. That is either a direct result of the conflicts (everyday life disrupted due to the ongoing fighting), or due to the use of the weapons as a means of robbing stores.

The illegal weapons come from a variety of sources. When it comes to international arms dealers, who usually sell to warlords or various militia, these weapons come either from previous, finished conflicts, or corrupt government officials who have the authority to order weapons for the national army. On the other hand, illegal weapons used by street-level criminals are usually either stolen from legitimate gun owners or bought by someone else who can legally buy a weapon and are then either given or sold to the criminal.

Counterfeit Goods

Counterfeit goods are estimated to be worth around \$250 billion per year, accounting, according to the World Customs Organisation, for 5-7% of the global merchandise trade⁵. The range of available counterfeit goods is nothing short of impressive: apparel, electronics, and even medicine, as well as many more kinds of products, are all available as counterfeits. Counterfeit goods have, perhaps, the most direct impact on the economy than all segments of the shadow economy. When a consumer decides to buy a counterfeit product, valuable income is lost from legitimate businesses. This decision is also often a misinformed one, since consumers are often tricked into buying them, mistaking them for the original product.

The effects of counterfeit goods are not only economic; these products are in many cases ineffective, or even dangerous, jeopardising as such the safety of the user. In the case of electronics, batteries of disputable origin have been known to catch fire or explode during use. The situation is even worse when it comes to counterfeit medicine, which, by some estimates, account for up to 10% of all medicine used worldwide. These drugs are labelled and appear identical to legitimate products, but have slightly different chemical composition, drastically reducing their production costs, but, at the same time, making them much more dangerous.

MAJOR COUNTRIES AND ORGANISATIONS INVOLVED

Portugal

Portugal is the only case where all the possession and consumption of all drugs has been decriminalized. The key word here is *decriminalized*. Since 2001, people found in possession of over a certain amount of a drug - an amount which differs for each drug - will have the substance confiscated and be forced (at least in some cases) to attend special “dissuasion panels”. Repeat offenders may also have some sort of treatment prescribed to them, such as regular psychological counselling or opiate substitutes such as methadone.

The policy, while internationally criticised at first, is now being seen as extremely successful. HIV infections in 2012 were down to 56 from 1016 in 2001, drug overdose deaths down to 16 from 80 in 2001, and drug-related deaths are down at 3 per million citizens, compared to the EU average of 17.3. The key to this success is pairing the decriminalization with strong harm reduction measures, such as counselling for drug users, methadone treatments, and needle exchanges.

An important problem with this policy, however, is that, on its own, it does nothing to affect the black market. While drug users are treated better by the state, they still have to get their drugs from illegal drug dealers, meaning that the black market remains largely unaffected. Yet, as a smaller part of the population is using addictive substances, the amount demanded (and hence supplied) is also smaller; in this case, while the measure was meant to help struggling drug addicts, it also managed to curb the sales of such substances in the illegal markets.

World Customs Organisation (WCO)

The WCO is an international organisation which aims to “[provide] leadership, guidance and support to Customs administrations to secure and facilitate legitimate trade, realize revenues, protect society and build capacity.”⁸. The WCO achieves its aims through the use of its various bodies including the Policy Commission which concerns itself with broad policy issues and the establishment of new policies, the Capacity Building Committee, which suggests new policies and tools for increasing the capacity of the organisation and the Council, the supreme body of the organisation which oversees all other committees. The organisation currently consists of 180 countries, accounting for over 98% of worldwide trade.

The WCO has the capability to propose new regulation and introduce new procedures and technologies, as well as the authority to oversee their adoption, making it the most effective way to control the flow of shadow economy products between nations.

Timeline of Events

| Date | Description of Event |
|----------------|---|
| 1976 | The Netherlands legalize the possession of small amounts of marijuana for personal use. The laws regarding marijuana established then are the ones active to this day |
| 9-20 July 2001 | UN Conference on the Illicit Trade in Small Arms and Light Weapons in All Its Aspects. The conference where the PoA was first drafted. |
| 2001 | Portugal decriminalizes the possession of all drugs. At the time, Portugal had a severe drug problem, with close to 1% of its population using heroin. The decriminalization was paired with harm reduction measures, such as counselling for drug users, methadone treatments, and needle exchanges. |
| July 2006 | UN small arms review conference to review the PoA. The conference did not result in any documents, and simply reaffirmed the existing PoA from 2001. |
| 2012 | The US states of Washington and Colorado legalize the recreational use of marijuana |
| 2014 | The US states of Alaska and Oregon legalize the recreational use of marijuana |

UN INVOLVEMENT: RELEVANT RESOLUTIONS, TREATIES AND EVENTS

Programme of Action to Prevent, Combat and Eradicate the Illicit Trade in Small Arms and Light Weapons in All Its Aspects (Programme of Action or PoA) (A/CONF.192/15)

The PoA is a UN Document, formulated in 2001 which aims to guide member states to reduce and ultimately eliminate the illicit trade of small arms and light weapons. The programme does not provide any binding measures, or aim to directly combat illicit arms trade; instead, it provides a variety of general guidelines for controlling illicit arms trade at the national, regional, and global level. The

solutions proposed in the document, could be used as-is or serve as a framework for the implementation of further solutions, specialised to specific countries or regions. This would simultaneously provide a basis for anti-illicit arms trade measures, and allow for the international coordination of these measures.

PREVIOUS ATTEMPTS TO SOLVE THE ISSUE

The war on drugs

The war on drugs was started in 1971 by US president Richard Nixon, following the rise of drug use during the 1960s. Nixon added marijuana to “Schedule 1” drugs, the category that is deemed to contain the most dangerous and highly persecuted drugs, ignoring the suggestion of a committee of his creation made to evaluate the legal status of marijuana. Use of the drug was shortly decriminalized on a state level for a period in the 1970s but those reforms were abandoned soon thereafter.

The policy has been widely criticised for its contribution to the skyrocketing of incarceration rates and increasing prison population, given that it allowed for the incarceration of even small-time drugs users, as well as the ever increasing cost of maintaining the policy.

The policy has also introduced the concepts of mandatory minimum sentences and zero-tolerance policies to the US judicial system. The former refers to the setting of an absolute minimum sentence that a court has to give to those found guilty of certain crimes, regardless of circumstances. The latter is the opposite of a tolerant policy which would allow for drug users to be caught in possession of drugs a small number of times. A zero-tolerance policy does not allow for that, and instead punishes offenders the first time they are caught.

In total the war on drugs has cost over \$1 trillion to the US government, and done almost nothing to reduce drug usage, or curb the black market. This goes to show that directly trying to combat the *effects* of the shadow economy is bound to fail. It is imperative, in order to reduce black market trade, especially in drugs, to find a different solution.

Decriminalization and legalization in the Netherlands/some USA states

Decriminalization and legalization are often seen as a way of curbing the black market. The idea is that if consumers have access to legal drugs, there will be no reason to turn to the black market, effectively transferring the profits of illicit drug dealers to legitimate, *taxable*, drug dispensaries. There are experts who believe that this is possible, however, the effect would not be immediate. What would happen is that the existing illicit drug market would slowly decrease in size and eventually reach the size of the illicit alcohol or tobacco market, both of which are very much alive, but much smaller than their legal counterparts⁶. What legalization in places like the American state of Colorado has shown is

that black market prices are difficult for legal, taxed, dispensaries to compete with, meaning that people will still turn to illegal drugs, even when legal options are available, as they are cheaper.

Certain previous attempts to legalize prostitution have been made, and they have brought by some reasonable concerns; these mainly involve the quality of life of the workers, and the fact that this line of work has been characterized as degrading for all human beings involved.

POSSIBLE SOLUTIONS

In your resolutions, you will have to propose effective and feasible solutions to control the black market on a regional, national, and global level, considering all the challenges that each different section presents. The most notable challenge with controlling the black market is perhaps cooperation. In order to control the global flow of illegal goods, nations have to cooperate and share information that is, in most cases, considered classified.

Legalization of illegal drugs, prostitution, and other illegal goods

This is a measure which, lately, has begun seeing wider acceptance. As stated above, legalizing illegal substances and putting them under government control would reduce the incentive for drug users to turn to the black market. There are, however, a variety of important considerations:

Firstly, the distinction between 'hard' and 'soft' drugs. While the legalization of marijuana (both of its use and sale) is becoming more and more prevalent, there is yet to be a country to legalize the sale of drugs such as crack cocaine or heroin. There is the example of Portugal, where the *use* of all drugs has been *decriminalized*, but sale remains illegal. The legalization of 'soft' drugs appears, at least in the short term that it has been applied, to have overall positive or, at the very least, neutral effects; but the legalization of all drugs is completely untested and undocumented, as well as finding very little public acceptance.

Even concerning marijuana only, there is the argument of legalization vs decriminalization. Simply decriminalizing cannabis can, on its own, have strongly positive effects by allowing drug addicts to be treated as patients instead of criminals and not burdening drug users with criminal records. It does not, however, have any effect on the black market, since people still have to obtain drugs illegally. Legalization has all the benefits of decriminalization, along with reducing the profits of illegal drug dealers, creating jobs, and providing a new source of income for the government.

As of lately, there have also been arguments for legalizing prostitution. The main argument is the worldwide the worth of prostitution is estimated at 186 billion dollars; all of which is undocumented and hence not taxable. It is suggested that this could be of immense financial benefit, yet due to the nature of the profession certain ethical concerns have been raised. It should also be noted, that in accordance to the religious beliefs of certain groups, it is likely that such a decision will

be met with heavy opposition. Therefore the extent to which prostitution should be legalized is up for debate.

Another issue with legalization comes in the form of light arms and counterfeit goods. Studies have shown that nations where the purchase of arms is easy and requires no background search, experience more mass shootings than those where the purchase requires a special permit, or is illegal. Hence a possible legalization of possession of all arms is likely to have severe social consequences. Counterfeit items should also not be legalized, as their existence is an infringement of copyright laws, as they simply mean to trick people into buying them.

Enforcing the PoA

The PoA already provides a large selection of possibly effective measures that could directly combat the illicit trade of small arms and light weapons. Its adoption, however, is extremely uneven, given that it is, at its current state, not much more than a suggestion. Making it mandatory or enforcing it internationally in some way, even if not in its entirety, would make use of the measures it suggests and put them to use in the real world.

It is also advisable that it is used as the basis for a new framework. While the core ideas of the PoA are applicable to all nations, it should be optimal if it underwent certain nation specific modifications, so as to counter the issues that each nation faces more accurately.

This idea does have its limitations, however, since it is not realistically possible for the UN to directly change national policy. The measures that would be enforced, therefore, would have to be severely limited to those that can be directly enforced by international organisations and those which find wide acceptance among member states, severely limiting actual effectiveness of the treaty.

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