Global Developments Around Tobacco Track and Trace and How They Relate to the US

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What This Presentation Covers

• About ITSA
• Illicit cigarette trade in US compared to rest of world
• Measures that could be used to curb illicit trade
• Measures that are being used and with what results
• Update on EU track and trace system (EUTPD)
• Recommendations and conclusions
About ITSA
About ITSA

• Formed 2015 by 10 founder members with a primary objective to promote a unified voice of the tax stamp providers and promoter of global standards.

• ITSA has the following 3 priorities:

1. Active role in developing ISO 22382 for tax stamps – published 2018 – targeting the content, security features, issuance and examination of excise tax stamps


3. Sharing of knowledge and expertise and advice to government authorities on their national excise management and related supply chain control programmes.
23 Members

3 HQs in North America,
1 in Latin America,
15 in Europe
4 in Asia.
1 member is a state security printer
Standards Organizations Collaboration

- ISO 22382:2018 – Tax Stamps
- ISO 12931:2012 – Authentication Solutions
Illicit Cigarette Trade
Comparison
US vs. Rest of World
Illicit Trade

### Estimates

**RoW**
- 10-12% global cigarette consumption
- $40-50 billion global tax loss

**United States**
- 7-21% total US cigarette consumption
- 1.24-2.91 billion packs
- $2.95-$6.92 billion tax loss

### Forms and Drivers

**RoW**
- Primary form: smuggling, incl counterfeiting and cheap whites
- Primarily foreign production
- Main driver: weak governance

**United States**
- Primary form: cross-state activity
- Almost all domestically produced
- Main driver: tax differences

Source:
Centers for Disease Control and Prevention 2015 report, Preventing and Reducing Illicit Tobacco Trade in the United States
Euromonitor International, 2015
State Cigarette Excise Tax Rates
Per 20-pack

Note: Federal excise tax is $1.01 per pack.
Measures to Eliminate Illicit Trade
Overarching Measures

- Recommendations presented by the CDC in its 2015 report and echoed by the World Bank, the Framework Convention Alliance, ISO standards, ITSA and the WHO Framework Convention on Tobacco Control

1. Adopt comprehensive federal approach with one agency leading efforts
2. Strengthen enforcement
3. Enhance federal, state and local surveillance and evaluation
Individual Elements of a Comprehensive Approach

- Federal Track and Trace program
- State-level ‘three-legged stool’ approach
- Federal and state public education
- Tribal tobacco policies

Source:
Centers for Disease Control and Prevention 2015 report, Preventing and Reducing Illicit Tobacco Trade in the United States
Definition and Benefits of Secure Track and Trace?

**Tracking**
- Systematic real-time monitoring of the movement of products through the supply chain

**Tracing**
- Occurs during or after enforcement action and involves reconstructing the flow of products to identify the point of diversion into illicit/licit channels.
What are the Core Functions of Track and Trace?

- Ability to verify quantity produced or imported
- Verify correct tax payments
- Track products through supply chain
- Trace products back to source
- Ensure product authenticity through the application of secure product markings at point of manufacture or distribution
Minimum Data Required

- Date and location of manufacture
- Manufacturing facility
- Intended market for retail sale
- Product description
- Secure unique identifier
Critical Elements of Track and Trace

- Real-time control on all production/distribution lines
- Track and Trace code activation on production/distribution lines
- Linking of SKU with Track and Trace code
- Push-button device for authenticating fiscal mark and product
US Federal Agencies who have the Authority to Implement a Federal Track and Trace System

- **FDA**
  - Family Smoking and Prevention Act of 2009

- **TTB**
  - Has FET collection authority; recommended to congress in 2010 “to work with the FDA on the development of any tobacco product tracing system so that the system can be used to the extent possible for enforcement purposes.”
Why Haven’t They Done It Yet?

- Federal Regulators struggle over the question whether a track-and-trace system should be a national system or one that is implemented by a State protecting its citizens and revenues.
- Although improving, low-tax states have historically had limited incentive to adopt track and trace
Individual Elements of a Comprehensive Approach

- National track and trace system
- State-level ‘three-legged stool’
- Federal and state public education
- Tribal tobacco policies
State-Level – Three-Legged Stool

Licensing

Product marking

Enforcement
Measures Currently Being Used and the Results
Tax Stamps with Traceability Function
MICHIGAN

- Holographic and Digital Security
- Unique Identifier for State Track and Trace
- Adopted 2014
Revenues increased by $15.7M (1.8%) 1st 12 months post implementation vs total revenues 12 months prior.

Revenues increased by $29.8M (3.4%) 1st 12 months post implementation vs forecasted revenues for the same time period under previous program.

Program self-funded through increased revenue. Investment in program paid back in less than 1 year.
ECUADOR

$7.64 MM increase
Tax Collection Mar 17 – Feb 18

58,000 tobacco packs
Seizures Mar 2018

244% More
Seizures than 2016 for spirits and tobacco

OVERT
- Colour shifting
- Fine line
- Latent Image

SEMI-COVERT
- Double polarization of colour shifting ink
- UV Ink

COVERT
- Forensic marker authenticated by specialized lab equipment

Aggregation & Track & Trace in Distribution Chain
Example of What Not to Do… INDIA

In 2013, Indian states of Uttar Pradesh and New Delhi transitioned from a holographic tax stamp to a plain label with a QR code and serial number for track and trace – but no physical security features – the number of fake codes soared.
At least 70 die in India after drinking spurious liquor - local media

Indian officials and local media say there are still several people falling sick after drinking cheap spurious liquor that already killed dozens of people, most of whom from the village of Balpur in Uttarakhand.
EU Track and Trace
Why EU System is not considered Best Practice

- No guarantee of security
- No guarantee of independence
### WHO Protocol vs EU System

<table>
<thead>
<tr>
<th>WHO FCTC Protocol</th>
<th>EU System</th>
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</thead>
<tbody>
<tr>
<td>Secure unique identifier</td>
<td>Unique identifier (but not necessarily secure)</td>
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<tr>
<td></td>
<td>5 security features that are separate from the unique identifier</td>
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<tr>
<td>Global information-sharing focal point</td>
<td>Each tobacco company selects and appoints primary data storage provider</td>
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<tr>
<td>No delegation of tasks to tobacco industry</td>
<td>Allows delegation of some tasks to industry</td>
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Key Areas of Concern With EU System

• EUTPD should not be considered as a blueprint
• Conflicts with Protocol by allowing key obligations to be delegated to tobacco industry – conflict with Article 8.12
• Independent third parties don’t have sufficient control over unique identifiers
• Data storage providers with historical links to industry appointed as part of system
• Security feature required to authenticate pack but not unique identifier – conflict with Article 8.3
• Only 1 out of 5 authentication elements must be sourced from independent provider
• Time stamp requirement adds complexity and little value in enforcement
Recommendations and Conclusion
ISO 22382 Recommendations

- Develop a track and trace system for tax stamps
- Use multi-layer security in tax stamps
- Don’t delegate key obligations to tobacco companies
- Do not rely on third party suppliers with links to tobacco industry developments
- Require that unique identifier includes only elements listed in Protocol, not longer list in EU system
The Basic Equation

TRACEABILITY + AUTHENTICATION = HIGH SECURITY + $ € £ Increased tax revenues

Traceability in itself is NOT Authentication
Thank you!