The illicit market in India is increasing at an alarming rate, in seven main sectors (two of which are alcoholic beverages and tobacco), according to a recent report by FICCI CASCADE (Federation of Indian Chambers of Commerce & Industry Committee Against Smuggling and Counterfeiting Activities Destroying the Economy).

Among these sectors, the maximum tax revenue loss, to both federal and state government, has come from tobacco, followed by mobile phones and alcohol products. Smuggled international contraband cigarettes have contributed significantly to the growth of the illegal cigarette market. There has been a sizeable influx of cheap smuggled cigarettes from countries like Bangladesh, China and Myanmar into India’s north-east region, which has thus become a distribution centre for the rest of the country. While the supply of legal cigarettes shows a decline, counterfeiters and smugglers have taken over this market which has been growing at a high rate.

In the case of alcohol, the illegal market has grown significantly, both in value and quantity, also in the north-east region, especially for IMFL (Indian-made foreign liquor) and imported liquor.

The continuous rise in the illicit trade of tobacco and alcohol is due to various reasons. These include high-taxed products, a complex tax structure and a considerable difference in tax rates between the various states of India.

The problem is not just a numbers one though. There are many other reasons for the continuous rise of illicit trade, including:

- The sheer size of the domestic market;
- Improper coordination among state police forces;
- Lack of knowledge and awareness among consumers;
- Non-usage of anti-counterfeiting solutions on product packaging.

The lack of adoption of complete tax stamp programmes is another key reason for the increase in the illicit alcohol market. States such as Karnataka and Puducherry have not yet implemented a complete tax stamp programme on all their liquor products. Moreover, states like Maharashtra, Bihar and Jharkhand are yet to implement solutions for product authentication and proof of tax paid. This situation offers further scope for liquor tax stamps to prove their significance.

As far as cigarettes are concerned, the scope is even larger, considering that tax stamps are not currently used at all on tobacco products in India (tobacco policy matters are governed by federal, as opposed to state law).

**Combined physical/digital tax stamp developments**

With a focus on authentication, many states have upgraded their tax stamps to the next level using combinations of new authentication features and digital technologies. For instance, the state of Andhra Pradesh has replaced paper labels with a high-security hologram carrying a 2D matrix/1D linear barcode-based track and trace system.

Each tax stamp carries an inkjet-printed serial number of up to 10 digits, and a 2D barcode holding up to 40 characters. The stamp includes a 4mm2 demetallised feature to accommodate the 2D barcode.

In another case, Chhattisgarh Excise Department has begun using a high-security hologram with SMS authentication via mobile phone.

These developments are based on the view that physical and sensory authentication tools are still required to support track and trace systems. For example, in some situations an examiner may need to verify a liquor bottle visually due to the unavailability of readers, or due to a power failure, or network failure or simply because of time constraints at crowded control sites. Electronic authentication is not possible everywhere, especially in remote areas, hence the requirement for instant visual authentication, such as that provided by a high-security hologram.

If we do not integrate both digital and non-digital (physical and sensory) authentication into our approach, then we risk wasting the major investments that are about to be made in track and trace.

**Developments specific to beer**

Recently, the Puducherry Excise Department decided to affix security holograms onto beer products manufactured in local breweries. The government also decided to import the security hologram into the Union Territory of Puducherry, as one measure to eliminate the sale of non-duty paid beer. (Puducherry first started using tax stamps on IMFL products in 2007-08, and the stamps contributed towards a 56% revenue growth.)

Meanwhile, in Delhi, two major breweries have implemented a fully automated production monitoring system, comprising high-speed stamp application, in-line unit-to-case aggregation, and a dispatch solution.

The system provides an effective way of carrying out production accounting activities without compromising production speed and efficiency. However, the beer market is reported to be less susceptible than hard liquor to tax fraud, due to its highly automated and controlled production environment and the lower retail price of beer products.

**Track and trace without enforcement won’t work**

The territory of Delhi (which also uses a label with 2D barcode for track and trace on liquor), offers a real-life example of why track and trace alone, without robust enforcement measures (and honest enforcement officials), will not be effective.

In April this year, nine excise officials were held in Delhi for liquor smuggling activities which had allegedly caused an estimated loss of INR 25 billion ($385 million) to the exchequer.

The track and trace system in Delhi calls for liquor products to be transported by the manufacturer (with a valid transport permit) to respective warehouses, where they are scanned and recorded. From there, the warehouses (also with valid transport permits) supply the products to liquor retail outlets. Excise officials deputed for the purpose must supervise the entire process.

However, enforcement authorities discovered that a major chunk of the liquor was not even going inside the warehouse after the barcode scan, but was instead being unloaded right at the gate and transported directly to liquor shops. The liquor was then being sold off as a priority, and the police were even reported to be issuing fake transport permits to ward off excise inspectors.

**Conclusion**

While the illicit market in India has dramatically increased, it is still possible to tackle illicit trade with some success.

Today, a total of 22 states (including three union territories in India) are using approximately 20 billion tax stamps per annum. According to various reports, as well as the Authentication Solution Providers’ Association (ASPA), the mandated use of tax stamps in states such as Uttar Pradesh, Tamil Nadu, Uttarakhand, Madhya Pradesh, Puducherry, and Chhattisgarh, have resulted in increased revenue collection.

The success of tax stamps in India comes from their dual role in supply chain monitoring and visual authentication of taxes paid, for both enforcement authorities and individual consumers. However this dual role needs to be supported by the appropriate organisation and regulation of the Indian liquor trade.