The State of Illicit Cigarettes in Sri Lanka

By Chander S Jeena, Secretary, Authentication Solution Providers Association

According to an academic report released in January, the Sri Lankan exchequer lost revenues amounting to LKR 18 billion ($102 million) in 2017, as a result of the illicit cigarette trade. The report states that 583 million illegal cigarettes, amounting to 15.57% of the total tobacco market, made their way into the Sri Lankan market in 2017 compared to just 4 million in 2016 – which is a massive leap.

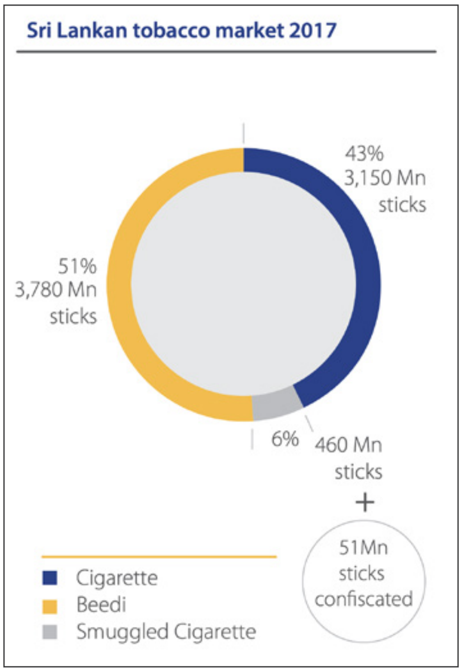
The report, titled *A Baseline Study on the Illicit Cigarette Market, and the Resulting Tax Implications for Sri Lanka*, was conducted by Dr S N Morais and Prof S S Colombage of the Open University of Sri Lanka Department of Social Studies, and Dr C N Wickramasinghe of the Department of Commerce and Financial Management of the University of Kelaniya. During the launch event for the report the question was raised as to whether it had been backed by local cigarette manufacturing interests, to which one of the professors enigmatically replied that a 'private consulting company' had funded the research.

According to Sri Lanka Customs (SLC) Director Mahendra Arthanayake, the number of illicit cigarettes detected by SLC increased by around 21% year-on-year in 2018. Prof Colombage pointed out that the lower than projected revenue from cigarette taxes is an indicator of the existence of a massive illicit market.

According to him, the realised budget revenue from cigarette taxes was 3.3% lower than the forecast, during most of the years between 2009 and 2017. 'It is noteworthy that the actual value was lower than the forecast value in six out of nine years, indicating the existence of illicit trade,' he said. He emphasised that tax increases alone wouldn't bring down cigarette consumption in Sri Lanka.

Interestingly, the report findings are in sync with those of the Ceylon Tobacco Company's (CTC) 2017 annual report, which estimates similar numbers. Sri Lanka's tobacco industry consists of CTC – the only legal manufacturer of cigarettes – as well as the under-regulated beedi market (a beedi is a type of cheap cigarette made of unprocessed tobacco wrapped in leaves), and the illegal cigarette market. CTC's market share has continued to decrease over the past decade or so as tax and other tobacco regulations have primarily targeted the legal industry, creating an unfair playing field.

According to its authors, the research report is intended to provide independent observations on the prevalence and consequences of the illicit cigarette trade in the country. The report calls on the government to adopt measures in line with the WHO FCTC Protocol, which Sri Lanka ratified in February 2016. The country does not currently have a tax stamp system in place.



Source: Ceylon Tobacco Company PLC Annual Report 2017.

India's Recent Hooch Tragedy Confirms TSTN's Concerns

By Chander S Jeena, Secretary, Authentication Solution Providers Association

The recent tragedy involving the death of over 100 people from consuming poisonous bootleg alcohol (hooch) in the Indian state of Uttar Pradesh (UP) and its neighbour Uttarakhand – has confirmed the concerns of *Tax Stamp & Traceability News*™ (TSTN) over the absence of physical anti-counterfeiting security features on the tax stamps used by UP.

As part of a move to implement track and trace technology in accordance with its 2018-19 excise policy, UP's Department of Excise replaced secured holographic liquor tax stamps with plain barcoded stamps devoid of any physical security. It is ironic that a state which was one of the first in India to adopt full-faced holographic tax stamps almost 17 years ago should also be one of the first to drop these stamps in favour of simple barcode labels. Indeed, TSTN already raised its concerns over these labels when the territory of Delhi adopted them a few years before UP, with negative consequences. One would have thought that UP would have learned from Delhi's experience, but apparently not (see also TSTN July 2018).

The lesson that should have been learned here was this: physical authentication features are still needed, in order to secure track and trace systems. If we do not integrate both digital and non-digital (ie. physical and sensory) authentication methods into our approach, then we risk wasting the major investments that are being made in track and trace.

Tax stamps are often thought of as simple tax collection structures, belying their potential value as a platform around which broader excise modernisation strategies can be developed. The existence of cheaper, less sophisticated, less effective stamps and marks potentially dilute their value proposition.

Now is the time for governments to change their approach towards this issue. Tax stamps – just like banknotes – require the highest levels of security that aid different stakeholders in authenticating the product, as well as the stamp.