



PHILIP MORRIS INTERNATIONAL

FIGHTING THE ILLICIT TRADE IN TOBACCO IN THE EU

DISCUSSION PAPER
JULY 2016

INTRODUCTION

As new legal frameworks emerge around the world to tackle the issue of illicit trade in tobacco, this paper is a contribution to the discussion around the most appropriate solutions for dealing effectively with this problem within the EU. It provides an overview of the various solutions available to decision makers in the implementation of Articles 15 and 16 of the Tobacco Products Directive, noting the current nature of the problem, the range of available systems and technologies, as well as existing production methodologies.

The paper presents a PMI perspective on these issues. This position incorporates the thinking of interested parties including supply chain participants, technology providers, manufacturers, Customs and other law enforcement agencies. It is intended to serve as a discussion paper that can contribute to an effective and lasting solution to the problem of the illicit trade in tobacco.

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The illicit tobacco trade is a significant global problem. According to KPMG, it accounts for up to 10.4% of the global cigarette market and more than 53 billion cigarettes in the EU alone.¹ Aside from the risks to consumers from purchasing illicit and unlicensed cigarettes, the impact on European tax revenues are substantial at an estimated €11.3 billion a year².

The economic, social and international security implications of the illicit trade in tobacco products are significant and include:

- Lost tax revenue for governments;
- Reduced effectiveness of public health policies;
- Threat to national security by providing a major source of illegal income for organized crime and terrorist organizations;
- Threat to the sustainability of the legal supply chain;
- Major impact on the legitimate industry's business activities and revenues.

The illicit tobacco trade has also become an increasing threat to global security, a point recently illustrated by the European Commission:

“The illicit tobacco trade has long been recognized as a main source of revenue for organised crime, and, in some cases, terrorist groups. The new European Agenda on Security adopted by the European Commission on 28 April 2015 recognizes the importance of fighting cigarette smuggling as a means of cutting off criminal groups from this revenue source.”³

This concern is shared by the US State Department:

“Like other forms of illicit trade, the illicit trade in tobacco products, commonly referred to as cigarette smuggling, is a growing threat to U.S. national interests. Internationally, it fuels transnational crime, corruption, and terrorism. As it converges with other criminal activities it undermines the rule of law and the licit market economy, and creates greater insecurity and instability in many of today’s security “hot spots” around the world.”⁴

It is also a business imperative for PMI to combat this problem and ensure its products are legally sold in the market for which they are intended. PMI loses significant revenues as a result of illicit trade as well as market share. It also damages PMI’s brands’ reputation.

> The problem today

Twenty years ago, contraband and counterfeit products of major tobacco brands were the the main issue. However major progress has been made to reduce this threat significantly. This success can be partly credited to a close cooperation between the tobacco industry, its supply chain, and government representatives such as law enforcement, customs and fiscal authorities. However new threats continue to appear, from sophisticated counterfeiting to the issue of 'illicit whites', unknown 'brands' typically without a legal distribution network in the EU.⁵

> EU agreements to tackle the illicit trade

Greater coordination and technical advances in tackling the illicit trade came about partly thanks to the cooperation agreements signed between individual tobacco companies and the European Union between 2004 and 2010. In PMI's case, it signed its 12 year Cooperation Agreement with the European Union and ten EU Member States in 2004. All EU Member States have since then joined the agreement.

¹KPMG, Project Sun, 2016 | ²ibid. | ³European Commission, Technical assessment of the experience made with the Anti-Contraband and Anti-Counterfeit Agreement and General Release of 9 July 2004 among Philip Morris International and affiliates, the Union and its Member States, 24 February 2016 | ⁴US State Department, The Global Illicit Trade in Tobacco: A Threat to National Security, December 2015 | ⁵European Commission, Technical assessment of the experience made with the Anti-Contraband and Anti-Counterfeit Agreement and General Release of 9 July 2004 among Philip Morris International and affiliates, the Union and its Member States, 24 February 2016

The provisions of this agreement have proven highly effective. In a recent technical assessment report by the European Commission, the PMI Cooperation Agreement was praised for its effectiveness, leading to a reduction of seizures in contraband of more or less 85% between 2006 and 2014. However, since 2004, the illicit trade has evolved, particularly with growth in unknown brands, or 'illicit whites' without a legal distribution network in the EU.⁶

The agreement between the EU and PMI expired on 9 July 2016 and the European Commission decided not to prolong it. Although the agreement was not extended, the supply chain control measures outlined in the agreement will remain an integral part of how we do business in the EU and around the world. With or without the agreement, our commitment to fight illegal trade around the world remains intact and stronger than ever.

> New legislation

In addition to the Agreement, provisions for tackling the illicit trade in tobacco are being legislated at an EU level with the drafting of the implementing acts of 2014's Tobacco Products Directive (TPD) articles 15 and 16, which address Track & Trace and the Security Feature. The content of these acts, which will specify how the principles of the directive are put into practice by EU Member States, is vital in determining how we address the illicit tobacco trade in the EU and offers both opportunities and challenges that will be explored in detail within this paper.

Additionally, at a global level, the process of ratification of the World Health Organisation's Protocol to Eliminate Illicit Trade in Tobacco Products, within its Framework Convention on Tobacco Control (FCTC) is taking place. The FCTC Protocol will complement the TPD in EU member states and it is important that the TPD reflects its principles. PMI supports the FCTC Protocol but, as with any treaty, ratification by a large number of States combined with proper implementation and monitoring will be the key to its success.

> Moving towards effective legislation

As a result, an opportunity exists to confront the issue of illicit trade more broadly, elevating the debate to address the most pressing current issues. These include the rise of small scale low-volume high-frequency smuggling, more sophisticated counterfeiting and, most significantly, the impact of smuggled cargoes of legally produced but illicitly traded 'illicit whites' from both inside and outside the EU.

This Discussion Paper advances this ambition. It seeks to promote a constructive and collaborative debate on the most appropriate and effective strategies and technologies to comply with the requirements of Article 15 and 16 in order to tackle this global issue within the borders of the European Union.

⁶European Commission, Technical assessment of the experience made with the Anti-Contraband and Anti-Counterfeit Agreement and General Release of 9 July 2004 among Philip Morris International and affiliates, the Union and its Member States, 24 February 2016 | ⁷Agreements with British American Tobacco, Imperial Tobacco, and Japan Tobacco International are due to expire in, respectively 2030, 2030, and 2022

The illicit trade in tobacco is made up of three distinct product categories:

Contraband: Genuine product smuggled and sold illegally

While large scale smuggling of PMI's products has declined significantly under the provisions made in the EU Agreement, PMI is now dealing with new challenges. These include repeated small scale cross-border smuggling, exceeding legal import limits, both from outside the EU and within the EU that takes advantage of price differentials between member states, and the smuggling of unaccompanied parcels through ports.

Counterfeit: Copies of genuine products, produced and sold illegally

Following a period of decline PMI saw a significant increase in counterfeit seizures of its products in 2015. Quality of the copies vary but have become increasingly sophisticated and often include fiscal markings.

Illicit Whites: Unknown brands, typically without a legal distribution network in the EU⁸

These are, for the most part, produced outside the EU and are manufactured to be then smuggled into and sold illegally in another market. The largest entries to the EU market come from Belarus but cigarettes that can be termed illicit whites are also produced within the EU⁹. Smuggling is typically by truck or containerised transport, with product either hidden or labelled for re-export. Sales of illicit whites rob Member States and the EU of tax revenue and place unregulated product in consumers' hands.

⁸European Commission, Technical assessment of the experience made with the Anti-Contraband and Anti-Counterfeit Agreement and General Release of 9 July 2004 among Philip Morris International and affiliates, the Union and its Member States, 24 February 2016 | ⁹Project SUN: A study of the illicit cigarette market, 2015

THE IMPORTANCE OF TRACKING & TRACING

Effective track and trace processes and protocols are an essential part of maintaining supply chain integrity. The term Track & Trace itself can be defined as the ability to track forward the movement of products through specified stages of the extended supply chain and trace backward the history, application or location of the product which is under consideration¹⁰. The systems currently in use in the tobacco industry are similar to those used by the pharmaceutical, high technology and chemical industries, as well as logistics providers, where it is also vital to ensure secure supply chains.

This information allows the industry to efficiently manage, control and secure supply chains. It also assists law enforcement authorities in identifying who has handled potentially illicit products and at which point these products left the legal supply chain.

Tracking and tracing therefore requires supply chain partners to record events related to objects under their control.

This means that:

- Manufacturers record the creation of products, the packing of products into higher packaging units, and their subsequent dispatch to their first customers.
- Distributors then record the receipt of products and their onward delivery to their respective direct customers.
- Information associated with these events, known as 'tracking events', is captured and entered into each company's database, from which relevant information is uploaded into a centralised event repository.

¹⁰GS1, Business Process and System Requirements for Full Supply Chain Traceability, November 2012

PREVIOUS COMMITMENTS - THE COOPERATION AGREEMENT

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> The EU Cooperation Agreement

On July 9 2004, Philip Morris International, the European Union and 10 of its member states signed a 12-year cooperation agreement, which by 2009 was ratified by all 28 Member States. The purpose of the agreement was to work together to tackle the issue of the illicit trade in PMI brands within the EU¹¹.

As part of the agreement, PMI was required to introduce stringent record keeping, rigorous screening of potential business partners and the eradication of cash payments, which has all resulted in the tightening of supply chains, making them more transparent. Additionally, as part of the agreement, PMI has provided €1.25bn in funding to the Commission and member states over the course of the agreement. The agreement proved successful in achieving much of its objective, with its provisions helping to achieve an 85%¹² decrease in seizures of contraband of PMI products.

Today, PMI's Fiscal Compliance Policy has global reach, far beyond the requirements of the EU Agreement. Also, over the last 5 years, cooperation between PMI and government agencies under the EU Agreement has led to:

- 37,000 PMI employees being trained in compliance with the EU Agreement;
- Signing of 12 Memoranda of Understanding with the EU law enforcement agencies;
- Delivery of counterfeit recognition training for nearly 7,000 law enforcement officers across Europe;
- Inspections of over 200 raided illegal factories in Europe alone.

Because the Agreement required the implementation of an effective tracking and tracing system, PMI was obliged to develop a digital coding system to meet the requirements of a high paced manufacturing environment. It has subsequently been adopted by the other leading tobacco companies, resulting in a significant positive impact on the reduction of illicit trade. The system, known as Codentify, is totally interoperable across the whole supply chain, as it is fully compliant with international standards on data carriers

and information exchange protocols. It is currently used in more than 120 countries worldwide to detect diversion and check validity of the codes. Over the last decade the system has been used to track and trace over 500 million master cases of cigarettes.

> Fostering an advancing technological environment

However, PMI is not in the track and trace business. Just like any commercial entity, PMI looks for the most effective and cost efficient system. As a result, rather than developing and implementing the technology itself, PMI would prefer an open standards based environment in which different organisations compete with each other to develop the most effective solutions to tackle the underlying issue. PMI believes that this approach would be the most appropriate mechanism to foster an advancing technological environment that would allow the industry and governments to always stay one step ahead of the criminals. To be clear, PMI does not want to continue to develop and invest in its own Track & Trace technology. PMI would prefer to be able to choose the best and most competitive technology that would allow it to tackle this issue most effectively.

> After the EU Agreement

The agreement between the EU and PMI expired on 9 July 2016 and the European Commission decided not to prolong it.

Although the agreement was not extended, the supply chain control measures outlined in the agreement will remain an integral part of how we do business in the EU and around the world. With or without the agreement, our commitment to fight illegal trade around the world remains intact and stronger than ever.

Articles 15 & 16 of the Tobacco Products Directive will reinforce efforts to broaden EU wide tracking, tracing and security authentication. This paper, considers how legislation can build upon the success of the EU Agreement and the measures already in place, to create an effective and lasting framework that fosters innovation, competition, and collaboration.

¹¹ Similar agreements were signed by the European Union and the member states with Japan Tobacco International (JTI) in 2007, and British American Tobacco (BAT) and Imperial Tobacco Limited (ITL) in 2010. | ¹² Technical assessment of the experience made with the Anti-Contraband and Anti-Counterfeit Agreement and General Release of 9 July 2004 among Philip Morris International and affiliates, the Union and its Member States

Any solutions to tackle illicit trade in the EU must be implementable within the framework of the regulatory landscape. With the EU Cooperation Agreement expired, attention has turned to the two key pieces of legislation that are being considered at Member State and Commission level. Firstly the European Tobacco Products Directive's implementing acts for Articles 15 and 16 and secondly the World Health Organisation's Framework Convention on Tobacco Control's Protocol to Eliminate Illicit Trade in Tobacco Products (FCTC Protocol).

PMI supports the aims and objectives of both these pieces of legislation. As stated, it is in PMI's interest to tackle the illicit trade in tobacco and PMI wants to support all efforts to do so, leveraging its expertise and global scale where appropriate.

> The Tobacco Products Directive (TPD)

At an EU level, the European Commission has rightly demonstrated just how seriously it takes the problem of illicit trade by including the issue in its updated Tobacco Products Directive. The Directive is an update of the original Tobacco Products Directive of 2001 and aims to improve the functioning of the internal market for tobacco and related products, while ensuring a high level of health protection for European citizens and addressing the issue of the illicit tobacco trade.

The Directive's implementing acts, which specify how the principles of the Directive can be practically applied, are currently being drafted, including on Article 15, which provides guidance on track and trace, and on Article 16, regarding security feature. These implementing acts will seek to clarify what processes and solutions are best placed to address the issue of effective tracking and tracing of tobacco products (Article 15) and how to apply security feature (Article 16) across EU Member States and supply chains.

The drafting of the implementing acts, which specify how these principles should be applied in practice, offers the EU and EU Member States opportunities, as well as challenges, in ensuring the legislation best addresses this global problem within the EU.


> The FCTC Protocol

(The World Health Organisation's Framework Convention on Tobacco Control's Protocol to Eliminate Illicit Trade in Tobacco Products)

Many of the measures implemented by PMI as part of its commitments under the EU Agreement have put to test the very same principles that are at the heart of the FCTC Protocol.

The Protocol is an international treaty that aims to eliminate all forms of illicit trade in tobacco products. It intends to do this through a package of measures to be taken by countries worldwide acting in cooperation with each other. The WHO describes it as "a global solution to a global problem", a holistic approach that PMI endorses.

On the supply chain controls, the FCTC Protocol is focused on preserving the integrity of the supply chain. This requires participants in the supply chain to take measures such as the implementation of a global regime on tracking and tracing to prevent diversion of tobacco products and the licensing of key components of manufacturing machinery to tackle all types of illicit trade. These measures are intended to promote responsible business conduct that must apply equally to all participants regardless of size. Securing the global tobacco supply chain will make it easier for enforcement authorities to potentially detect both the point where products are diverted to the illicit market, and the criminals who trade in them.



The Protocol also provides for the legislative and enforcement aspects of dealing with the illicit trade problem. It outlines guidance for governments in terms of measures to deal with unlawful conduct including prosecutions and sanctions for criminal activity as well as liability. It covers the searching of premises and seizure of evidence, confiscation of assets, seizure payments, destruction of seized products and investigative techniques.

Finally, the FCTC Protocol calls on all Parties to cooperate with competent international organizations, as mutually agreed, in the sharing of a wide range of enforcement information and best practices, and with regional organisations to provide training and technical assistance in scientific and technological matters.

PMI fully supports the FCTC Protocol and its objective, and welcomes its ratification by the European Union and its member states, as it is a tool to address the serious problem of the illegal, unregulated tobacco trade. While it contains many of the measures that were within the EU Agreement, its global reach is aligned with PMI's commitment to tackling this problem in every market where PMI operates. PMI believes it would encourage universal application, creating a level playing field to tackle a broader range of issues beyond the scope of the TPD, such as the issue of illicit whites.

It is critically important that implementation of Articles 15 and 16 should remain focused on its primary objective, which is to eliminate the illicit trade of tobacco across the EU, as well as ensuring alignment with the objectives of the FCTC Protocol.

On a practical level, there are a number of core principles that should guide the implementation of Article 15 and 16. In particular, effective tracking and tracing requires open standards that are interoperable, independently monitored and supervised, and do not interrupt the manufacturing environment.

Based on PMI's global experience of working with multiple stakeholders across different jurisdictions, as well as its consultation with key stakeholders so far, PMI believes that the implementing acts of Article 15 & 16 can only be effective in reducing illicit trade if they take into account the following key factors.

> Article 15: Track and Trace

Open standards

Any future system needs to be based on open standards, guaranteeing they can be used by all relevant stakeholders in the supply chain across different technological platforms, geographies and products. This means that public authorities should clearly set out the requirements to which any proposed solution should answer, and allow competing providers to develop the most appropriate technologies to best tackle the problem. Market participants can then choose the most appropriate technologies based on cost-efficiency, technology and the best possible integration into the production and distribution processes.

Standards suited to production requirements

While open standards are important, the right sort of standards are also critical. For example, GS1 standards are followed by industries and organizations as diverse as the UK National Health Service and the World Customs Organization. GS1 has a million member companies across the world, executing more than five billion transactions daily

using GS1 standards.¹³ In addition to the dot-code, which GS1 is in the process of standardizing, PMI has the capability for creating and sharing visibility events using GS1's Electronic Product Code Information Services (EPCIS), the data matrix as a data carrier and the barcode; all effectively implemented and self-regulated by the industry.

PMI currently uses for tracking and tracing purposes an encrypted unique identifier that is suitable to the high paced production environment that you find in the tobacco industry. This is critical because for the TPD requirements to be successfully implemented, it requires a system that is appropriate for this environment using laser and/or inkjet printers to apply the unique identifier in a limited space on a unit packet.

Open competition between different solution providers

The positive competitive pressures inherent within an environment based on open standards will drive innovation and, together with other proven supply chain control measures (such as due diligence of logistics partners), will allow the brand holders and public authorities to stay ahead of the criminals. A technical framework that facilitates free competition and technological innovation among solution providers, whilst abiding by EU and WHO regulations, should be a first principle of any solution. Free market competition between different technology providers offers the best incentives for technological innovation and state of the art solutions.

Geographical interoperability

The TPD by definition only covers the EU but the problem of illicit trade is a global one. In fact many of the illegal products are derived from operators originating from outside of the EU. According to the European Commission's technical assessment of the EU Agreement "[t]he illicit tobacco trade is a main source of revenue for organized crime, and, in some case, terrorist groups. The new European Agenda on Security adopted in April 2015 recognizes the need to cut off criminal groups from this revenue source."¹⁴ It would be futile, and against the measures highlighted in the FCTC Protocol, to introduce a system unique to the EU that is not interoperable with others systems operating around the world.

¹³<http://www.gs1.org/about> | ¹⁴European Commission, Technical assessment of the experience made with the Anti-Contraband and Anti Counterfeit Agreement and General Release of 9 July 2004 among Philip Morris International and affiliates, the Union and its Member States, 24 February 2016

A solution beyond just tobacco

Tobacco is not the only product that suffers from illicit trade. Any system that is implemented must be interoperable with the solutions already in place within different industries to ensure ease of use across the supply chain, retail and law enforcement. In that respect, it should mirror similar directives applicable to the pharmaceutical and defence industries.

Independence and transparency

PMI fully supports calls for greater independence of tracking and tracing systems from the industry to ensure transparency across manufacturers' operations and to ensure the authorities have oversight over illicit trade. PMI agrees that transparency needs to be guaranteed so that both manufacturers and law enforcement have full visibility to detect the points of diversion in the supply chain. Access to tracing information can be enabled via various means, and current systems have been designed to provide many levels of supervision to government agencies, including oversight of the unique identifier generation and appointing independent third parties to supervise logistic data. PMI is open to choose the most effective solution, and encourages the same principle of transparency that the current system provides.

Adequate outside oversight

Track and trace solutions must be based on verification, not trust. The TPD envisages track and trace solutions being independently audited by a third party. PMI completely agrees that it should be the responsibility of an independent auditor approved by the Commission.

> Article 16: Security Feature

Article 16 of the Tobacco Products Directive requires that all unit packets of tobacco products carry a tamper proof security feature, composed of visible and invisible elements.

The purpose of all anti-counterfeit features is to enable the authentication of an item by industry, investigators, and ideally the wider public. The second function is to create a deterrent to anyone considering counterfeiting a product by making it difficult, costly and near impossible to evade detection and prosecution.

There are many anti-counterfeit technologies available to manufacturers and brand owners, ranging from the simple but effective, through to the highly sophisticated and extremely secure. While many different solutions exist, technologies can be broadly classified as follows: visible features, hidden or invisible markers, forensic techniques and serialisation / track and trace.

A layered approach

PMI favours a layered approach to security features, by which it means a variety of different measures all working in conjunction with each other, in order to present the most insurmountable obstacle to criminals. In line with the requirements of Article 16, manufacturers should have to choose which security feature they use from a repository of independently verified options. Manufacturers should then be required to work with wholesalers, distributors and the authorities to ensure that the supply chain is informed about the security features deployed to protect against counterfeiting.

Competition and Innovation

Product security features have undergone considerable improvement in recent years. Continuous innovation is key to keeping one step ahead of the criminals, so it is critically important that Article 16 provides a framework that can harness future development. The worst outcome would be if Article 16 led to the adoption of one or two static security features, shutting the door on future innovations and making it easier for criminals to master and beat the system. Competition, innovation and a layered approach to security features are key to keeping ahead of the counterfeiters.

In some Member States the tax stamp is one of the most familiar security features for cigarettes and will continue to have a role to play in the future. However, the effectiveness of this visible security feature has been undermined by examples of it being counterfeited or diverted onto illegal products. Tax stamps are, at best, one of a number of security features that could be deployed in a layered approach, drawing on the growing range of visible and invisible security measures on the market.

Current solutions available

Visible features enable end users to verify the authenticity of a pack. Examples of visible security features include colour shifting inks, holograms and security graphics, which are expensive to replicate and rely on complex manufacturing techniques, as well as sequential product numbering which provides a semi-visible security feature linked to Track and Trace.

Such features can help end users be aware of whether they are purchasing genuine product, but this does require education to be truly effective. Furthermore, counterfeiters have in the past developed copies that are sophisticated enough to confuse the average user. Therefore, these visible features are best used as an additional secondary security feature.

The most reliable security features are those that are invisible and are designed to enable only the brand owner and relevant authorities to identify counterfeited product. Examples of the technology used include invisible inks, embedded or hidden images, digital watermarks and even forensic technology which relies on laboratory testing of chemical, biological or DNA taggants within the pack fibres. The sophistication of the equipment required to authenticate these measures varies but many are suitable for on-site verification using appropriate technology. These features are not easy to detect or copy without specialist knowledge, and accordingly their details have to be controlled on a “need to know” basis. If compromised or publicised, invisible features lose a large degree of their security value. The general public will not be aware of its presence and nor will they have the means to verify it.

Invisible security features offer a much greater opportunity to develop solutions that cannot be replicated by those involved in the illicit trade. Manufacturers should be encouraged to apply invisible markers across their entire range of products and markets. However, legislation should not limit the security feature to only one or two solutions, as

this would significantly increase the risk of counterfeiting. Serialisation straddles Track & Trace and the Security Feature and combines visible and invisible security elements. It involves assigning a unique identity to each stock unit during manufacture – as part of the Track & Trace function - which then remains with it through the supply chain until its consumption. This identity will normally include details, such as the product's name, the lot number and expiry date – although in current use this takes the form of a unique pack coding which enables access to the same information held in a secure database.

An accredited approach

To enable the above multi-faceted approach, a clear framework is required that allows solution providers to compete and innovate and manufacturers to select solutions that best meet the needs of a particular product or market. For example the need to provide both visible consumer authentication and hidden security features to assist authorities in fighting crime.

We would propose that the implementing acts of Article 16 allow for an approach that catalogues approved solutions and allows for manufacturers to source multiple solutions, including visible and invisible features, from those identified by a central body as fully compliant with the Article. Innovation is a key driver in the security sector, with new technologies being introduced regularly. As such, a flexible approach is required that allows these constant improvements to be implemented by manufacturers following their approval and acceptance by a review authority.

Fighting the illicit trade in tobacco is not a battle that will be easily or quickly won. The organisations and individuals behind illicit trade are a serious threat to national security, involved in organised crime and terror financing, and responsible for millions of Euros of lost tax revenue.

The solution should necessarily be based on collaboration between all parties using a combination of strict control of the supply and distribution chain; the use of best-in-class innovative technology to identify, track and follow genuine product from production to distribution; and finally the education of key stakeholders and the broader public about the dangers and consequences of the illicit trade.

PMI fully supports the objectives of Article 15 and 16 of the TPD and believes that they can only be achieved if the implementing acts promote a framework of open standards that allow interoperability and innovation in the solutions applied. A supporting structure of control and auditing is required to ensure consistency and best practice across the industry, including smaller manufacturers who may need different solutions that meet their needs. Experience has shown that it is impossible to know what advances may be made in tracking and tracing technology in future years. The Directive must allow for innovation to continue to be part of the solution.

It is also a global problem that does not stop at the EU's border. Indeed much of the illicit tobacco on the EU market enters Member States from outside the Union, whether as counterfeit, illicit whites or contraband. Accordingly, PMI supports the ratification of the FCTC Protocol as a way to ensure a global response and level playing field for all stakeholders.

Technology plays a crucial role in combatting contraband, counterfeit and tax evasion. However, because illicit product found in one country is often produced in, or moved through, another, for it to be truly effective it must enable cross-border connectivity between different systems deployed at the national level. This should be complemented with international cooperation, deterrent penalties and a level playing field for all manufacturers.

Securing the manufacture and distribution of excisable products within and across national borders requires that different technologies can 'talk' to each other.

Interoperability between the systems used by law enforcement and trading partners can only be achieved if common, widely-endorsed IT systems and scanning equipment are used and internationally recognised standards for exchanging data agreed to.

In practice, technology can only be effective in fighting the issue of the illicit tobacco trade if it addresses these factors:

- Enabling law enforcement and trading partners to exchange information on a global basis so they can identify where products may have been diverted from legitimate channels, regardless of the brand owner, place of manufacture and final destination;
- Allowing all parties concerned to play their role in the fight against counterfeit products. This is done partly by offering the general public easy tools to distinguish between genuine and counterfeit products without the need of specialist inspection equipment. But also required are hidden security features only accessible to the brand holder and relevant authorities.

Our core principle is a belief in open and effective standards for Tracking and Tracing, that ensure interoperability, are independently monitored and controlled, and do not interrupt the manufacturing environment. With regard to security features, we believe that manufacturers must be able to choose a layered approach, selecting solutions from a framework of accredited different technologies.

The illegal trade in tobacco is evolving rapidly as criminals change and adapt their methods. Confronting this complex and multi-headed hydra with a static, closed solution, based on imposition rather than cooperation will fail. Winning the war against the illicit trade demands smart and effective cooperation between relevant stakeholders, which can promote continuous innovation. This paper has drawn from extensive discussions with the supply chain, solutions providers and with law enforcement and other government representatives. The solutions and structures outlined here are based on the continuous innovation and cooperation that is required to make them workable, effective and able to stay ahead of the problem.

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