International Tax & Investment Center

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SpecialReport

The Development of Modern Revenue Controls on Alcoholic Beverages

Executive Summary

Tax stamps are used by regulators in approximately fifty countries globally (see Annexe A for list of countries) in an attempt to protect alcohol tax revenues. This report assesses the effectiveness or otherwise of such systems and takes a closer look at the factors critical to determining the overall success of tax stamps and related technologies.

We show that, in isolation, tax stamps are a sub-optimal policy choice from both an efficacy and efficiency perspective. Instead, the goals of curbing illicit trade in alcohol and protecting tax revenues require a much wider package of effective monitoring, control and enforcement measures. High and discriminatory rates of tax should also be avoided as these incentivize illicit trade.

At best, modern electronic stamps may make a positive contribution where they are an integral part of a much wider system of enforcement and deterrence, and where the tax system is well-designed. But it is also possible for stamp schemes to be counter-productive. For example, the ability to counterfeit stamps and re-fill stamped bottles may allow illicit product to be more easily passed off as genuine. And the schemes can add significantly to costs in the legitimate industry, thereby exacerbating price differentials with unregulated products and incentivizing illicit activity in much the same way as high tax rates.

More specifically, the evidence highlights a number of factors that impact their effectiveness:

- The extra costs imposed on business creates upward pressure on prices. This serves as an incentive for some to avoid regulated channels – a counterproductive outcome of tax stamps;
- Stamps can be susceptible to counterfeiting and additional processes are often required in order to prevent other fraudulent practices such as the refilling of stamped products with illicit alcohol;
- Stamps embedded with a means of electronic communication may help the authorities identify legitimate product in the distribution chain and enable verification by consumers. In certain circumstances they have been associated with reductions in illicit activity and an increase in tax revenue for government. However, these impose considerable costs on legitimate business and involve the development and maintenance of complex logistic and IT control networks in order to be effective.

Before introducing any anti-illicit alcohol strategy, authorities should ensure that they have a full understanding of the size and nature of the illicit market. Successful anti-fraud strategies must be, ideally, evidence-based and targeted to the nature of fraud in the market, and implementation will depend heavily on well-designed and well-resourced surveillance, interception and deterrence activities. Indeed, if enforcement is sufficiently robust (and the tax system well designed), then potentially costly tax stamp schemes could be avoided altogether, with little revenue impact. Furthermore, in some circumstances, tax stamps will have little or no effect on illicit trade.

It follows that governments considering the introduction of a new stamp scheme should carefully examine whether alternative policies could achieve the same or even better results at a lower cost. That may mean stricter controls on licensing, more sophisticated systems of surveillance and control, enhanced penalties for illicit activity, awareness campaigns aimed at potential suppliers and consumers of illegal

A report by:

OXFORD ECONOMICS

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alcohol, and/or more resources for the revenue, border and police authorities. Effective controls also require a partnership approach across all enforcement agencies nationally and internationally, and can be enhanced by a partnership approach with legitimate businesses and trade associations.

Furthermore, whatever systems of enforcement and control are put in place, governments should also remember the potential for elevated tax rates to encourage informal activity at the expense of the formal tax-paying sector, thereby undermining revenues and encouraging the range of other problems associated with illicit trade, from irresponsible drinking to the funding of wider criminal activity. The overall structure and the tax base are important considerations too. A simplified, non-discriminatory alcohol tax structure set at reasonable levels will help encourage compliance and ensure transparency for both taxpayers and governments.

The seven case studies in this paper illustrate a number of the points referred to above:

- In Denmark, the government abolished tax stamps on spirits in 2015, having previously removed stamping requirements on wine in 2001. Stamps were widely considered to be outdated and unnecessarily burdensome and costly in terms of administration to manufacturers, importers and the Danish authorities alike. Viewed as a simplification of tax administration, the Danish government signed off on the abolition and agreed with industry that the requirement was one of the past and not in keeping with modern best practice.
- Turkey's tax stamp scheme is partially credited with helping to reduce illicit trade. But more recently, illicit trade appears to have been recovering, with many blaming sharp rises in tax rates and tighter regulations affecting taxed products.
- In South Korea, a scheme involving radio frequency identification (RFID) tags has been introduced for whisky-based products only. This has added considerably to costs for both industry and the authorities and has not prevented legal sales volumes and associated tax revenues declining.
- In the UK, illicit activity in the spirits market fell following the introduction of a scheme covering that category. However these were introduced as part of a much wider package of enforcement measures and views vary significantly on the role of the stamps.
- In Kenya, the introduction of electronic stamps is regarded as having some benefits in terms of combatting illicit trade, but costs to industry have become a great concern. It is, however, too early to judge the effectiveness of the scheme's more recent extension to beer, which has exacerbated the cost impact.
- In Colombia, despite a longstanding system of tax stamps for spirits, consumption of smuggled and artisanal products has remained stubbornly high with legal spirits consumption falling.
- In Morocco, the introduction of an advanced tracking system is credited by some with containing illicit activity although it is not possible to detect a positive impact in relation to beer, wine and spirits. Against a background where the cost of taxed and regulated alcoholic products is very high relative to that of artisanal and smuggled products, legal consumption of alcohol has fallen in recent years, accompanied by a decline in tax revenues.

Overall our review highlights that tax stamps make a limited contribution to achieving their intended policy goals such as tackling illicit trade, growing revenue and building consumer confidence. To work well, the evidence base first needs to be established on the illicit market and tax stamps should not be considered in isolation of other important policy levers including tax policy and a fit for purpose regulatory and enforcement framework.

Success in curbing illicit trade and ensuring tax compliance will be assisted, and to a large extent facilitated, by the following:

- Ensuring that the excise duty system is well designed – simple, non-discriminatory and set at reasonable levels;
- Setting excise duty rates at a level that means the difference between the cost of taxed and untaxed products does not provide a significant incentive to shift into the informal market;
- A broad strategy to tackle fraud in the industry that includes a robust understanding of the illicit market based on credible and comprehensive data, a well-resourced monitoring and enforcement regime and sufficient penalties to deter the demand for and supply of illegal product; and
- Where tax stamps exists, ensuring that tax stamps are difficult to counterfeit, and that procedures are in place to prevent other potential abuses of the stamp system. This needs to be appropriately balanced so that additional and unnecessary costs from the introduction of tax stamp regimes are minimised as much as possible for legitimate tax-abiding industry players.

1. Introduction

In line with tobacco and automobiles, the sale of alcohol has long been subject to excise taxation, charged on the production or sale of specific products. Unlike customs duty, which is charged at the border when products are imported, excise duties are charged 'inland', typically on the sale or the production for sale of the relevant good.

Products which are subject to excise duties tend to be characterised by their inelastic consumer demand—when price goes up, demand for the product falls less than proportionately—as this makes them good candidates for raising revenue. To maximise that revenue governments have often set high rates of excise duty for such goods.

Though overall demand may remain high in face of higher prices, reflecting the inelasticity, such policies very often lead to an increase in illicit trade as consumers seek alternative (cheaper) sources of supply for their desired products. In this way, setting excise rates excessively high will likely result in unintended fiscal and social consequences. For example, without effective forms of control, high rates of tax can result in a greater incidence of smuggling, non-declared domestic production, and greater use of counterfeit goods and illicit goods. As well as fuelling crime, this can have negative health implications (counterfeit alcohol can be hazardous to public health, for example), higher enforcement costs, and a reduction in the revenues collected, which is often the motivation for the introduction of excise taxes in the first place.

The term illicit alcohol covers a range of situations including smuggling, tax evasion, and counterfeit. The OECD definitions of terms relating to the illicit alcohol market are set out in the box. The type of illicit alcohol and the product involved varies from market to market. It follows that the most effective measure should be guided by the actual problem, and that a generic approach is unlikely to be effective. A guiding principle in introducing a tax stamp system should be that it is targeted to the problem, effective, proportionate and avoid significant disruption to legitimate business.

Governments have adopted a range of measures designed to ensure that taxes are paid and that illicit trade is minimised. More recently against an increasing emphasis on safeguarding health and intellectual property rights, and on consumer's interest in the provenance of consumable products, governments are seeking mechanisms that can also authenticate the goods and enable better tracking. . The result is that in certain jurisdictions tax stamps have been implemented to meet these multiple objectives - with questionable success.

This paper seeks to provide an assessment of the relative merits of tax stamps drawing on the experience of a select group of countries in which they have been used as a means of addressing illicit consumption. We begin by reviewing the varying types and technologies of tax stamps before providing an empirical assessment of their effectiveness via a case study approach. Finally, we provide an assessment of alternative and/or complementary means of tax and enforcement that can help to minimise tax evasion on excisable products.

Illicit trade in alcohol: definitions

The definitions set out in the 2015 OECD report "Charting Illicit Trade – Converging Criminal Networks", for alcohol not reflected in the official statistics of the country of production, the country of consumption, or both, include:

Informal alcohol:

- Beverage alcohol produced outside a regulatory framework, whose production and consumption tend to follow cultural and artisanal practices. Includes home production.
- May be licit or illicit, depending on the laws governing a particular jurisdiction.

Contraband/smuggled alcohol:

- Alcohol with original branding that has been illegally imported / smuggled into a jurisdiction and sold, evading tariffs / customs. This includes:
- "Ant-smuggling": circumventing import / export regulations by continuously exploiting exemptions that allow travelers to carry minimal amounts of alcohol for personal consumption. The beverage alcohol is purchased inside one jurisdiction where excise tax is lower than in the market where it is transported for commercial purposes.
- Beverages brought in excess of the applicable travellers' allowance regulation.

Counterfeit alcohol: Fraudulent imitations of legitimate branded products. These beverages violate the intellectual property (IP) rights of legitimate producers. Includes refilling, falsification and tampering.

Tax leakage: Legally produced alcoholic beverages on which the required excise tax was not paid in the jurisdiction of production.

Non-conformed alcohol: Products that are not compliant with production processes, guidelines or labelling legislation. Includes products produced with denatured alcohol or illegal industrial alcohol.

Parallel imports: Authentic, branded products licitly imported into, and sold in, a market without the consent of the brand owner.

Surrogate, or substitute, alcohol: Alcohol or products containing alcohol not intended for human consumption as beverages, but that are consumed as substitutes for beverage alcohol.

2. Tax Stamp Types and Technologies

What are tax stamps?

The use of tax stamps became widespread in the 19th century as a way, primarily, to collect taxes and fees. Stamps are issued by national and local governments and by official bodies of various kinds to indicate that a tax, duty or fee has been paid or prepaid (or in some cases that it is recognised that tax is due). Usually, a producer will buy stamps from the government to the value of the duty owed, which are then affixed to each bottle of alcohol or packet of cigarettes to show that excise tax has been paid.

Tax stamps come in many sizes and take many forms—they may be gummed, perforated, printed or embossed. Often the stamp will be fixed across a seal, so that on opening the pack or bottle the stamp is destroyed, to guard against re-filling.

Effectiveness of tax stamps

The design of both the tax stamp and the overall system can make an important difference to the effectiveness of the regime.

In some circumstances a tax stamp system may actually increase the scope for alcohol-related fraud. For example, the efficacy of tax stamps are called into question if the stamps themselves can be easily counterfeited or the nature of the products are such that they are susceptible to counterfeit through refilling of illicit product or other means. Any stamping and/or associated production processes therefore need to guard against these possibilities.

It follows that most paper tax stamps use highly specialised design features to guard against counterfeiting, along the same lines as for bank notes using the same type of paper and ink. Regrettably, experience has shown that even modern versions of paper tax stamps can be counterfeited, sometimes within weeks of their issue.

To keep ahead of potential counterfeiters, stamps are regularly updated with technological improvements, including multiple security devices intended to prevent counterfeiting. The downside to this approach is that costs can be high for administration and enforcement agencies, as well as industry.

Therefore achieving the right balance of robustness versus cost implications is important in the establishment of an effective tax stamp system. A costly system undermines the revenue raising effectiveness of stamps and/or increases the price of legitimate products. In the UK, production costs have been kept down by allowing stamps to be incorporated into the bottle's normal label, but this does nothing to prevent illicit re-filling and the authorities have to rely on other aspects of the enforcement and monitoring system to guard against this.

Further, the rise of computerisation and the ability to track payments accurately have made the use of tax stamps as a revenue collection mechanism in developed countries less common.

The following case studies explore the effectiveness of tax stamps in more detail.

3. Case Studies: The Effectiveness of Tax Stamps

At the outset, it is important to acknowledge that a major difficulty with assessing the impact of tax stamps is the lack of available information on:

- the size and nature of the illicit alcohol market at the time a tax stamp system is introduced, or changed,
- a lack of information about alcohol tax revenues and volumes, and
- a failure to undertake robust post implementation assessment of the system.

Ideally, this evidence base needs to be established to comprehensively assess the efficacy of tax stamps. We recognise, however, that there is limited information available in many markets, particularly regarding the incidence of the illicit alcohol market. As such, it is this paper's recommendation that this analysis is undertaken by markets before any meaningful consideration of tax stamps as an effective policy tool.

Notwithstanding the above, the following case studies are an attempt to examine and evaluate different tax stamp regimes based on the best available data. The profiles are informed by industry information and data, through interviews with industry representatives on the ground, and information and data in the public domain. It also includes data from the World Health Organization (WHO), for which the standard measure is pure litres of alcohol consumed by resident individuals aged 15 and over.[1]

[1] In the WHO dataset, 'recorded consumption' is that known about through trade, production, and distribution records, which will have attracted tax in the country. 'Unrecorded consumption' will not have borne tax there. This category includes home-produced alcohol and personal imports, whether legal or illegal, as well as all forms of smuggled, bootlegged and illegally-produced drink, and any other instances in which licensed distribution channels have been avoided.

3.1 Denmark

3.1.1 Background

Tax stamps for wine and spirits had been a longstanding feature of the Danish system. But they were abolished in the case of wine in 2001, and eventually ceased to apply to spirits in 2015. Prior to that, two types of stamp had been operational—a paper strip stamp applied over the top and one side of the bottle, and a specially stamped 'fiscal cap'. In practice, the bespoke complexities of operating the 'fiscal capping' machinery meant that the vast majority of imported products used the paper strip versions

The decision to phase out tax stamps altogether followed on from a proposal by the Business Forum (an independent advisory body), motivated by a feeling that the system had become antiquated and imposed an unnecessary and material administrative burden on both manufacturers and importers.

The decision to remove the system was the consensus view within Europe, with most member associations of the European Spirits Organisation supporting the removal of strip stamps, reflecting concerns that they contravened the spirit of the European Single Market, their perceived ineffectiveness as a means of control and the additional costs associated with their implementation.

3.1.2 Cost impact for the industry

By general consensus, the introduction of tax stamps raised costs for producers, with a disproportionate impact on small businesses. For example, a paper by the Scotch Whisky Association[2] pointed out that the requirement to apply strip stamps (of the type used in Denmark) reduced the efficiency of bottling line machinery by between 8 percent and 30 percent and raised the overall cost of operating standard bottling processes on automated lines by between 7 percent and 10 percent.

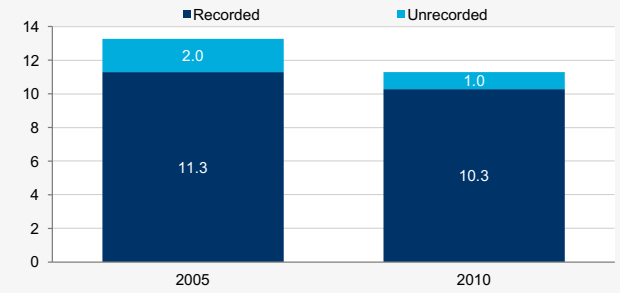
On top of this, firms were required to incur a significant capital expenditure cost with price of stamping machines ranging between €50,000 and €235,000. Moreover, there was evidence to suggest that the per unit operational cost of implementing tax stamps fell with production volumes. This would suggest that tax stamps impose a relatively more damaging impact on smaller producers, and are potentially anti-competitive.

3.1.3 Effectiveness in curbing illicit trade and impact on legal alcohol consumption

According to data from the WHO there was a significant drop in unrecorded alcohol consumption between 2005 and 2010. However, this was part of a wider decline in alcohol consumption over that period, with recorded consumption also declining, so the precise contribution of the tax stamp regime to the reduction in illicit use (if any) is unclear. In fact WHO data point to a 9 percent decline in recorded consumption volumes per head between during that five year period, led by a 19 percent decline for legal spirits—which were the only category of drink covered by the stamp regime at that time.

Recorded and unrecorded consumption of alcohol in Denmark

Pure litres of alcohol consumed per person aged 15 and over

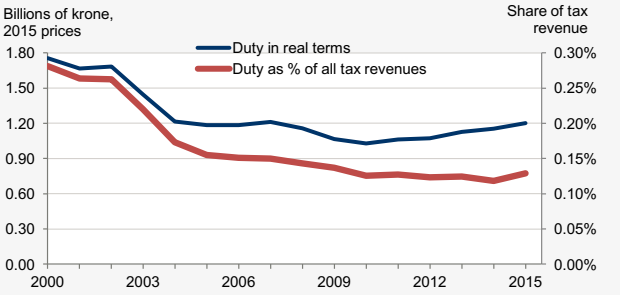


Source: World Health Organization

3.1.4 Impact on government revenues

While illicit trade fell significantly during the period in which tax stamps were in operation, recorded consumption also eased back and there was no positive impact for tax revenues. Indeed spirits excise duty revenues actually fell in inflation-adjusted terms, although that largely reflects a 45 percent cut in duty rates in 2003. While the resulting 25 percent drop in consumer prices was initially followed by a sharp rise in the level of recorded consumption per capita, this trend subsequently reversed.

Excise duty revenues from spirits



Source: Oxford Economics/Eurostat

After 2004, excise duty revenues held steady. At the time of writing, there is no data available that will help us to assess the potential impact of the abolition of tax stamps on revenues.

[2] Scotch Whisky Association, "Position paper outlining scotch whisky sector concerns regarding the duty and tax stamp regimes applicable to scotch whisky and other spirits in EU member states", October 2011.

3.2 Turkey

3.2.1 Background

Strip stamps were introduced for all alcoholic drinks in Turkey in 2006, when illicit alcohol use was high as a share of total alcohol consumption (though not in absolute terms, by global standards). They were replaced by 'next generation' stamps in 2015—offering information to consumers via a mobile phone application. Once the stamps are activated, the Ministry of Finance and relevant Regulatory Board are able to monitor the movement of the products through the distribution chain.

The stamps appear to have been successful in reducing illicit trade and unpaid taxes in the years immediately following their introduction, but more recently illicit activity is reported to have been on the increase in response to significant increases in tax rates. This underscores the point that, at best, tax stamps will only ever form a part of an effective tax and regulatory structure designed to minimise illicit consumption and maximise revenues.

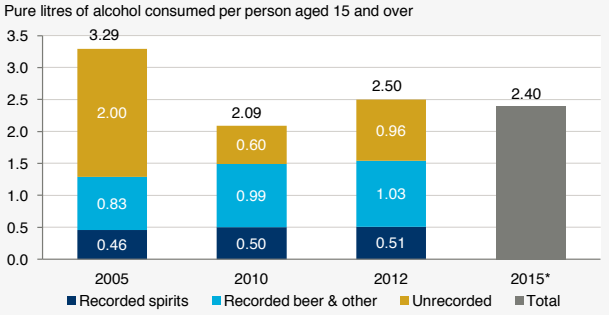
3.2.2 Cost impact for the industry

Stamps are fixed to each bottle either on site by local manufacturers, or by importers at the border. The costs of the machinery needed to attach stamps is covered by the company to whom the scheme is outsourced (although this is effectively incorporated into the cost of the stamp). The cost impact for domestic manufacturers is lower as the process of fixing the stamps can be integrated into the wider production process. However, importers face higher costs as they need to unpack and repack bottles in order to fix the stamps.

3.2.3 Effectiveness in curbing illicit trade

In terms of effectiveness, the period since 2006 in Turkey has two distinct phases, with a pattern of improvement and then reversal reflected in the figures published by the WHO. As the figure below shows, untaxed consumption declined between 2005 and 2010. The Turkish alcohol industry credits the introduction of tax stamps with reducing illicit activity in these early years, not least because no other anti-illicit trade measures were introduced around the same time.

Recorded and unrecorded consumption of alcohol in Turkey



Source: World Health Organization

* Projection. Consistent with unrecorded use of 0.95 litres if recorded use were the same as in 2014 (1.45 litres).

More recently, however, illicit trade appears to be increasing, as shown in the data where WHO estimates point to a clear rise in unrecorded consumption between 2010 and 2012.[3] This picture is reinforced by anecdotal evidence of a more recent and ongoing increase in illicit trade in alcohol.

The most likely explanation for this reversal, and a view shared by credible sources in Turkey, is the set of stark policy changes made in recent years. Alcohol tax rates have risen at a sharp pace, such that in 2015 the price of a popular brand of Scotch whisky was 52 percent higher than five years earlier (compared with a rise in general consumer prices of only 46 percent[4]). In addition, new restrictions on when, and where, alcohol can be sold, alongside a ban on all advertising and promotion of alcohol within the country's borders were introduced in 2013. This suggests that any positive impacts of the stamp scheme in curbing illicit activity may have been offset by the negative impact of the wider tax and policy environment.

3.2.4 Impact on legal alcohol sales

As the figure above also shows, the decline in untaxed consumption between 2005 and 2010 was accompanied by a modest rise in taxed consumption per head. Industry figures meanwhile show legal beer sales rising by 13 percent in that time, to nearly 900 million litres, with legal sales of spirits up by 10 percent to 66 million litres, and legal sales of wine up by six percent to 100 million litres.

However, since 2010, legal sales have fallen back as illicit trade has increased. Between 2010 and 2015, beer volumes fell by 10 percent. Although sales of taxed spirits edged up by four percent and legitimate sales of wine increasing by seven percent, the overall impact is consistent with taxed alcohol per head (on the WHO basis) falling by broadly six percent over the five years.

[3] It should be stressed that while the industry accepts the pattern shown in the WHO data is accurate, it regards the absolute level of illicit trade portrayed in that dataset to be vastly overestimated.

[4] All prices and sales volumes quoted in the case studies are based on Oxford Economics analysis of International Wine and Spirits Research (ISWR) data.

3.2.5 Impact on government revenues

The increase in legitimate alcohol sales following the introduction of tax stamps was followed by an increase in revenues from the 'special consumption tax' on beverages, from 0.21 percent of GDP in 2008 to 0.33 percent in 2012 (a trend which would also have been helped by gently rising tax rates). However, despite the sharp increase in tax rates since then, this ratio only edged up to 0.35 percent over the three years to 2015.

3.3 South Korea

3.3.1 Background

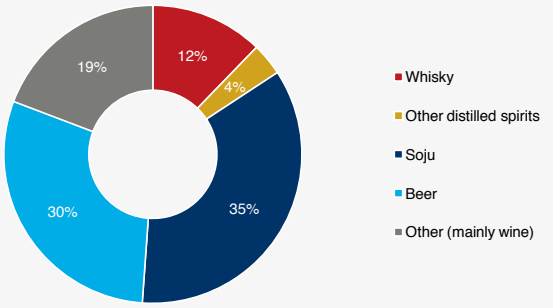
No stamp scheme existed in Korea until 2010, when a scheme consisting of RFID tags fitted to bottles was introduced to counter illicit trade in whisky products. The scheme was phased in gradually for the whisky market between 2010 and 2013, and coverage was extended to lower-alcohol whisky-based products in early 2016. The system remains confined to these drinks only.

With WHO data suggesting that whisky accounts for only four percent of recorded alcohol consumption in terms of pure litres of alcohol, and industry sources confirming that whisky sales account for broadly 12 percent of taxed sales by value, the impact of the scheme on the overall alcohol market has been limited. In addition, there is no data available relating specifically to the illicit whisky trade. However, we have gathered insights on the scheme's impact via discussions with industry players.

In general, while the scheme is believed to have helped curb the amount of illicit trade, several industry players have expressed concern about costs, which are not insignificant.

Breakdown of the market for alcohol in Korea

Approximate share of sales by value in 2015



Source: Oxford Economics estimates based on IWSR data and other industry sources

3.3.2 Cost impact for the industry

Tags are manually fixed by the manufacturer or importer and scanned by a reader. For the industry, the scheme's introduction necessitated the costly purchase of new machinery and the fixing of tags through a labour-intensive process—with imports having to be unpacked, tagged and re-packed. Some players do consider an upside in that the tags provide data on sales, make the market more transparent, and foster cooperation between the authorities and legitimate business. More often than not smaller industry players take a less positive view, as the proportionate cost of fixing the stamps is higher because they often have to resort to contracting out the process.

3.3.3 Effectiveness in curbing illicit trade

Prior to the scheme, counterfeiting of whisky products was not seen as a major problem, but an illicit trade in genuine products was believed to have taken place. Industry insiders believe that the scheme has gone some way to helping to restrict this illicit trade. This is partly because the tags provide information to the central authorities, with transmission of information taking place at the time that the tags are fitted as well as at the wholesale and retail stages of distribution. Counterfeiting of the tags is more difficult than if it were a traditional tax stamp, and the possibility of refilling tagged bottles with illicit product is made more difficult by the required process of bottle 'closure' as the tags are fixed. It also helps that consumers in Korea are familiar with the scheme. The tags can be read by consumers at restaurants and other outlets using special scanners which must be installed on the premises (though they cannot as yet be checked via a smartphone application).

3.3.4 Impact on legal alcohol sales

Despite the view that illicit trade has been curbed, legal sales of whisky have been in decline, falling from 22.6 million litres in 2010 to 15.8 million litres in 2015. However, this is simply a continuation of a longer term trend, with sales having peaked at 31.8 million litres in 2002. Prices have been relatively stable, with the price of the most popular brand of Scotch rising by just 9 percent over the last five years, which was only slightly below the 10 percent rise in consumer prices generally.

3.3.5 Impact on government revenues

Liquor tax revenues relating specifically to whisky declined from 265 billion Won in 2010 (0.15 percent of central government tax revenue) to 171 billion Won in 2013 (0.08 percent of central government tax revenue). This absolute decline was halted in 2014, as revenues increased marginally to 172 billion Won. However, without later time series data on the evolution of volumes or turnover it is not possible to gauge what effect RFID system has had on whisky related tax revenues.

3.4 United Kingdom

3.4.1 Background

The UK tax stamp scheme came into effect in late 2006 in response to concerns about undeclared imports of genuine brands. The implementation of tax stamp technology was subject to an EU tender process and the supplier is supervised by the Her Majesty Revenue and Customs (HMRC) procurement section. The use of tax stamps by individual manufacturers is subject to a highly complex set of arrangements.[5] Control of the use of tax stamps, and ensuring the compliance of manufacturers with these regulations, form part of the overall duties of the excise audit team. The audit team assume responsibility for revenue control of taxable products supplemented by regular and unannounced physical checks. All the main aspects of HMRC's revenue control system are described in Annexe C.

The scheme applies only to beverages with an alcohol content of 30 percent or more—so in practice almost exclusively spirits—and only to bottles of 35 cl or more. Since the scheme's introduction, illicit consumption of spirits has fallen, while legal sales of spirits, and associated duty revenues, have risen. However, the precise contribution made by the tax stamps to this picture is unclear, as a wider set of enforcement policies has been introduced during the past decade.

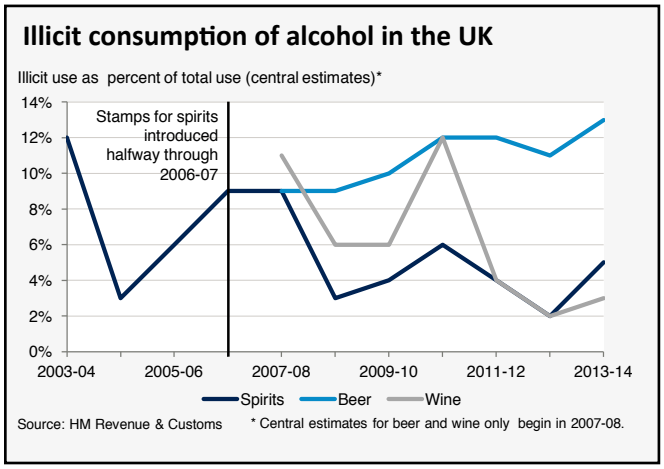
3.4.2 Cost impact for the industry

In some cases, the manufacturers or importers have the choice of incorporating the tax stamp into the bottle's main label keeping costs lower than otherwise, but set-up costs were still regarded by the industry as significant, with ongoing costs still seen as such by smaller manufacturers. An additional consequence of the incorporation of stamps into bottle labels is that stamped products cannot be exported, reducing the flexibility of producers in managing stock.

3.4.3 Effectiveness in curbing illicit trade

HMRC produces estimates of illicit alcohol consumption, separately for spirits, beer and wine, together with the associated tax shortfalls. These estimates suggest that the government's anti-illicit strategy has been successful in recent years, in the case of spirits. For that category, the average share of the market accounted for by illicit use was 10.5 percent in the six full fiscal years prior to the scheme's introduction (on HMRC's 'central estimate'), compared with 4.7 percent during the seven subsequent full years.

However, although the picture is a positive one, it is unclear how much of the reduction in illicit consumption of spirits can be attributed to tax stamps, which unlike those in Korea, for example, have no kind of electronic tracking system. As the chart shows, the general decline in illicit use of spirits since 2007-08 has been broadly matched by a decline in the case of wine, to which stamps do not apply.



Rather, the recent successes in holding down illicit consumption of both spirits and wine are likely to be more directly related to the government's wider anti-fraud strategy. This has included the digitisation of warehousing declarations and alcohol movement records; the use of due diligence and the Alcohol Wholesaler Registration Scheme to tackle criminal threats; liaison between the authorities and firms to make legitimate supply chains more secure; the tightening of regulations to reduce opportunities for fraud; and the strengthening of HMRC's fraud detection resources. More than 330,000 litres of illegal spirits were seized in 2015-16, with a revenue value (duty plus VAT) of £4.3 million. Although that is small compared with the remaining tax gap (£250 million for spirits duty plus VAT, for 2013-14), the fall in illicit activity is consistent with activities of this kind having a considerable deterrent effect.

Many within the industry argue that strip stamps have made little, if any, contribution to the reduction in fraud, and would prefer the system to be ended due to its costs.

Finally, it is worth noting a recent rise in estimated illicit activity in the market for beer. As a result, the shortfall in beer, wine and spirits duty revenues together fell only from 10.3 percent in 2007-08 to 7.6 percent in 2013-14, whereas that for spirits and wine alone more than halved, from 9.6 percent to 4.2 percent. Estimates and projections published by WHO, meanwhile, suggest that total unrecorded alcohol consumption (based on litres of pure alcohol) in the UK fell from 9.7 percent of the market in 2005 to 8.6 percent in 2012, but may have nudged back up to above 11 percent by 2015. Some industry experts have suggested therefore, that the policy of applying the scheme to spirits but not to beer, where illicit trade has become more of a problem, is inconsistent.

[5] See https://www.gov.uk/government/publications/excise-notice-ds5-uk-duty-stamps-scheme for more detail.

3.4.4 Impact on legal alcohol sales

Since the introduction of the scheme, legal sales of spirits have risen from 249 million litres in 2005 to 289 million litres in 2015. That 16 percent rise compares with growth in the population aged 18 or over – the legal age for purchasing alcohol in the UK – of 9 percent. That has been achieved despite significant price rises, partly related to increases in duty. The cost of the most popular brand of vodka increased by 57 percent over the 10 years, compared with a rise in the general consumer price level of only 25 percent.

3.4.5 Impact on government revenues

HMRC's estimates of the percentage shortfall in excise duty closely follow the share of illicit consumption in the market. Helped by the downward shift in the latter, spirits duty revenues increased by a cumulative 36 percent in real terms between 2005-06 and 2015-16, to £3.15 billion, whereas the relevant rate of excise duty was raised by 18 percent in the same period.

3.5 Kenya

3.5.1 Background

The history of tax stamps for alcohol in Kenya falls into three phases. The system was extended from tobacco to spirits in 2006, in an attempt to curb the significant amount of illicit use and associated tax losses. But the stamps had no electronic function and were not difficult to counterfeit, and illicit trade remained widespread. This prompted the introduction of new electronic stamps in early 2013, as part of the wider Excisable Goods Management System enabling stamped products to be tracked and validated. But the effectiveness of that system, in terms of reducing illicit trade, remains unclear and disputed. Finally, in early 2016 the system was extended to cover all alcoholic drinks including beer.

3.5.2 Cost impact for the industry

The tax stamp and tracking systems have added significantly to costs, taking into account the installation of stamp fixing equipment, the fixing process, the cost of the stamps themselves (which are charged for on top of excise duty), machine downtimes associated with the system, system management, and meetings with officials. The costs are borne by the industry with no help from the government, but in practice they are passed on to the final consumer.

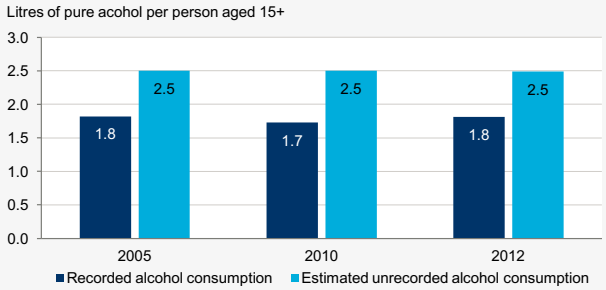
The industry's concerns about costs were compounded by the extension of the scheme to beer. In the six months following this move, the cost to a key industry player is put at one billion Kenyan shillings (US $10 million). This includes the cost of stamps for drinks of all types, and losses associated with significant machine downtimes, but it mostly relates to beer. Beer production in Kenya is currently running at around one billion bottles per year (400 million litres, mostly in 0.5 and 0.3 litre containers). With each stamp charged at 1.5 shillings, the annual cost of the stamps alone, for Kenyan beer manufacturing operations, will amount to 1.5 billion shillings (US $15 million). Consequent price rises are then magnified by the impact of VAT.

3.5.3 Effectiveness in curbing illicit trade

According to the WHO, untaxed consumption accounted for the majority of alcohol use in 2005, with the picture remaining similar in 2010 and 2012. Continued illicit use at that time involved undeclared production, inward smuggling, 'flow back exports', and counterfeiting. The fact that the original tax stamps were 'mute' made them less effective in countering these activities, while counterfeiting of stamps, and the fixing of genuine stamps to counterfeit products, are believed to have exacerbated the problem. This illicit activity is believed to have centred on spirits rather than beer.

The system introduced in 2013 will have made it easier to identify and deter illicit activity. The new stamps have enhanced security features as well as electronic function. A track and trace accounting system is now in place enabling licenced manufacturers and importers to order, pay for and activate the stamps, and enabling the Kenya Revenue Authority (KRA) to approve orders and analyse activity. The KRA also set up the Market Surveillance Unit, with 100 officers recruited in 2014, on the way to a target of 300. Devices were introduced to enable these officers, as well as manufacturers, distributors and retailers, to validate stamps, and tens of millions of shillings-worth of illicit products, including spirits, have since been seized and destroyed. Advertising campaigns are now run, and consumers can validate stamps using smartphones, and report suspicious products via a hotline.

Recorded and unrecorded alcohol consumption in Kenya



Source: World Health Organization

Even so, the practical impact on illicit trade is as yet unclear, and disputed. No WHO data on untaxed use is available post-2012, and while the KRA points to a sharp rise in revenue collection (see below), industry representatives do not believe that the system has been particularly effective in curbing illicit trade. Illegal and

potentially dangerous home-brewed alcohol, consumed on site in 'secret dens', is believed to have remained common. Illegal imports of spirits may continue to be encouraged by the existence of lower-priced products elsewhere in the East African customs union. And there is also a view that it is only a matter of time before the new stamps are counterfeited. Regarding beer in particular, industry officials believe that illicit trade was never a problem, and that extending stamps to these products has simply pushed up costs and prices for no good reason.

3.5.4 Impact on legal alcohol sales

According to the WHO dataset, taxed consumption remained steady, at close to 1.8 litres of pure alcohol per head, throughout 2005-2013. That is consistent with the tax stamp system doing little to encourage switching from illicit and informal consumption to formal consumption at that time. More recent ISWR data is consistent with legal consumption of spirits picking up on a per capita basis between 2013 and 2015, and with beer and spirits sales holding up at historically high levels in 2016.

However, the industry does not believe that the stamp system has contributed to recent buoyancy—indeed, it is thought that sales would have been higher still had it not been for stamp- and excise-driven price increases, especially in the case of beer. Instead, it is put down to wider economic growth benefiting sectors of all kinds, investment in the market by international stakeholders, and a review of tax on alternative alcoholic drinks made from sorghum. To the extent that some spirits consumption may have switched from the illicit to the legal market in 2015 and 2016, this is put down to increased anti-illicit activity by the authorities and the formal industry, rather than the stamps themselves.

3.5.5 Impact on government revenues

It is widely accepted that the original 'mute' tax stamp system did little to curb illicit activity. Indeed total excise duty revenues declined from a peak of 3.2 percent of GDP in 2005-06 to 2.0 percent in 2011-2012.[6] The position since the introduction of the track and trace system is unclear, with the KRA stating that revenues relating to tobacco, spirits and wine jumped by 40 percent after the system's introduction. But while total excise duties rose in cash terms from 79 billion shillings in 2011-12 to 140 billion shillings in 2015-16, as a share of GDP they have only risen to 2.1 percent.

Most recently, increased rates of duty for beer and soft drinks, imposed in late 2015, are expected by the authorities to bring in 17 billion shillings per year, with a further 30 percent boost to revenues from these items due to the extension of tax stamps to them. But whether these extra revenues are realised, or sustained, remains to be seen, given the potential for higher prices to suppress beer sales.

3.6 Colombia

3.6.1 Background

Colombia has a longstanding system of tax stamps. All imported and domestically-produced spirits, spirits-based ready-to-drink products (RTDs), and wines, require a consumption tax stamp specific to the department (regional authority area) in which the drink is to be sold. Despite this, the illicit share of total alcohol consumption has remained stubbornly high, with growth in the legal market subdued in recent years and associated tax revenues depressed as a consequence. The federal authorities have announced an intention to introduce a national 'track and trace' system in response, but the timeline for implementation, and other key details, have yet to be confirmed.

3.6.2 Cost impact for the industry

While the stamps themselves do not have to be paid for, over and above the excise duty payment that they signify, the wider system nevertheless involves significant costs. The stamps must be affixed over the closure of each bottle, with one international company running 20 warehouses across the country where manual fixing takes place. In addition, payments have to be made for legal documents allowing the transportation of imported alcoholic products, and the company pays a logistics partner to undertake the significant amount of paperwork associated with the payment of excise duty. No financial help is given by the authorities.

Taking other costs into account too, Colombia is regarded by the industry as one of the most expensive countries in the world in which to operate. And while the cost of complying with the legal framework is not significant on a per bottle basis for large scale operations, it can be for smaller operators in the legitimate market.

3.6.3 Effectiveness in curbing illicit trade

Despite the tax stamp system, illicit trade is fairly widespread in Colombia. This is encouraged by the comparatively low affordability of alcoholic products, taking local earnings into account, and the availability of lower-priced alcohol in neighbouring countries. High rates of excise duty, the system of departmental-run monopoly alcohol retailers ("licoreras"), and the associated restricted availability of legally-imported products, are all blamed for contributing to this picture.

Total alcohol consumption is estimated by WHO to have been close to the global average, at just over six litres of pure alcohol per head, in 2010 and 2012.

[6] Including tobacco as well as spirits and beer—no breakdown is available. The fiscal year runs from July to June.

But the proportion accounted for by unrecorded use was around 30%, which was little changed on 2005 and clearly above the global average of 24 percent. Euromonitor also find the illicit share of the total to be fairly high by global standards.[7]

Illicit alcohol trade is reported to mostly involve spirits rather than beer or wine, and to include smuggled imports (such as from Venezuela, Panama and Aruba), counterfeiting, and the manufacture of illegal and potentially dangerous adulterated spirits. Smuggled products are often channelled through the La Guajira special customs zone, while some counterfeiting involves adulterated spirits being bottled in recycled, originally-genuine containers. Organised criminal gangs are reported to be heavily involved in all of these activities. Euromonitor suggest that counterfeit alcohol accounted in 2014 for 46 percent of the illegal market by volume, and contraband (i.e. illegal imports) for 36 percent, with alcohol not intended for human consumption (10 percent), illegal artisanal products (five percent), and evasion of duty by otherwise legal products (three percent) making up the remainder.

The tax stamps are regarded by the industry as easy to counterfeit. In addition, a black market exists allowing smugglers and counterfeiters to get hold of genuine stamps, and genuine original bottles, bearing genuine stamps, have been found to have been refilled. So while consumers are able to check the validity of stamps by visiting a website, this is not sufficient to guarantee the legitimacy of a product. More generally, the legitimate industry believes that government enforcement activities could and should be stepped up, with the penalties for illicit activities strengthened. Implementation of the proposed federal tracking system would be welcomed as part of a wider enforcement effort.

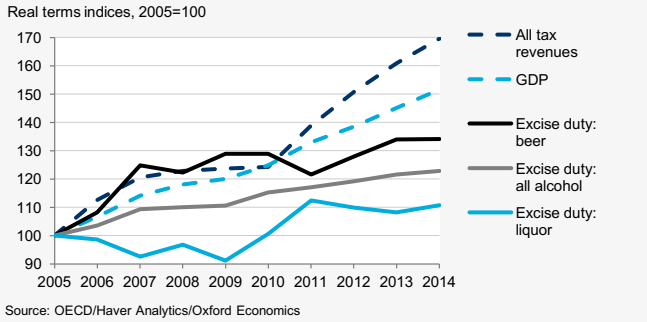
3.6.4 Impact on legal alcohol sales

Recorded alcohol sales are reported by WHO to have been fairly steady on a per capita basis, at around 4.5 litres of pure alcohol per head, throughout the period 2000-2014. The market mainly comprises beer and spirits, with legal beer consumption rising over that time but legal use of spirits – which are the subject of the tax stamps regime – declining on the WHO basis. The Euromonitor report suggests that legal sales volumes grew more slowly than illicit volumes between 2012 and 2014, while ISWR-based estimates point to subdued growth in legal sales between 2012 and 2015, with legal spirits consumption dropping in the latest year.

3.6.5 Impact on government revenues

The Colombian authorities suffer significant tax losses as a result of contraband and counterfeit alcohol, with the same Euromonitor study for example putting fiscal losses at US $423 million in 2014. As alcohol-related excise duties collected in that year amounted to just over US $1,500 million, this loss is clearly significant in proportionate terms.

Trends in tax revenues relative to GDP



Source: OECD/Haver Analytics/Oxford Economics

With growth in the legal market constrained, alcohol-related taxes have fallen relative to both overall tax revenues and GDP. Between 2005 and 2014, OECD data show the total of all tax revenues in Colombia increasing by a cumulative 70 percent in inflation-adjusted terms, ahead of the increase in real GDP of 50 percent. But alcohol-related excise duties grew by a comparatively modest 23 percent on that basis, only just ahead of the 19 percent rise in the adult population. Excise duty on beer rose by 34 percent in real terms in that time, while duty on liquor was up by just 11 percent, with no growth at all after 2011. Consequently, alcohol duties fell from 2.7 percent of all tax revenues in 2005 to 2.0 percent in 2014, having accounted for 4.0 percent as recently as 1999. For those departments owning and running "licoreras", the continued high level of illicit spirits use, at the expense of legal spirits purchases, will also depress non-tax state revenues.

3.7 Morocco

3.7.1 Background

Morocco introduced a new sophisticated tracking system in 2012, aimed at countering illicit trade in excisable goods of all kinds and shoring up associated tax revenues. Alcoholic drinks are covered by this system amongst a much wider range of products.

While the country has a comparatively low level of alcohol consumption, WHO estimates point to the share of illicit use in that total still being comparatively high in 2012, despite a clear drop compared with 2005. Since 2012, the new tracking system is credited by some experts with reducing illicit trade, and associated tax avoidance, for excisable products in general. But for alcoholic drinks specifically, the formal industry nevertheless remains concerned about both smuggling and artisanal production. Tracking system-related costs, as well as tax rises, are blamed for pushing up the price

[7] Euromonitor International for SAB Miller, "The illegal alcoholic beverages market in six Latin American countries 2014" (2015).

of taxed and regulated drinks, relative to their informal counterparts, resulting in a fall in the consumption of formal products and alcohol-related tax revenues.

3.7.2 Cost impact for the industry

Industry sources suggest that the combined cost of recent tax rises and implementation of the secure tagging system forced local beer manufacturers to raise selling prices by between 12 and 25 percent. Taking into account information on recent tax rises and selling prices, the tax element appears to account for around half of this extra cost, suggesting that the cost of implementing the tagging system alone has added some 6-12 percent to the prices charged.

3.7.3 Effectiveness in curbing illicit trade

WHO estimates suggest that unrecorded consumption was comparatively high as a share of total alcohol consumption in 2012, albeit lower than in 2005. The excisable goods tracking system introduced since then, meanwhile, is well regarded by experts in the revenue protection field, and credited with pushing illicit trade down and holding revenues up, at least with regard to this group of goods in general.[8]

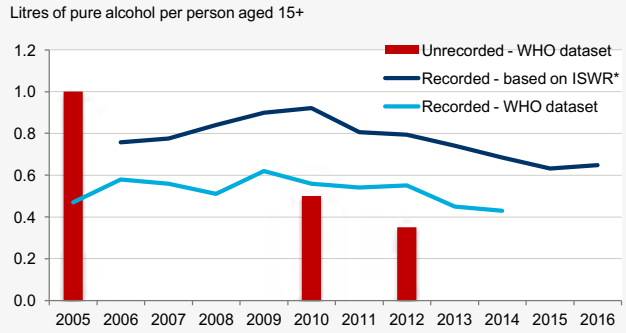
But despite this, the formal alcohol industry remains concerned about both smuggling and local artisanal production (which may be legal or illegal but on which no tax is paid). Smuggling is reported to be rife in Northern Morocco, away from the country's main industrial centres, with some reports of 70,000-100,000 smugglers traveling daily to and from the Spanish enclaves of Ceuta and Melilla. Illicit imports are also reportedly sourced from Gibraltar and the Canary Islands. Smuggled product is estimated by the industry to be in the region of 4-5 million litres per annum, for beer, wine and spirits together—equivalent to as much as four percent of legal market volumes.

Artisanal production meanwhile is reported to be a substantial 50 million litres per annum, which could be as high as 40 percent of total legal alcohol sales volumes. These products are much more affordable than those imported legally or produced locally in the formal sector, with a typical 70cl bottle of spirits-strength alcohol costing around four dirhams or less, compared with over 70 dirhams for an equivalent bottle produced by the taxed and regulated sector. As well as avoiding tax, suppliers of these products also avoid the cost of complying with regulated production and bottling standards, and the labelling is often misleading. Artisanal products sold in the more remote regions typically bear counterfeit tax stamps, but those sold in shopping malls tend to bear genuine stamps.

3.7.4 Impact on legal alcohol sales

While the impact of the new tracking system on illicit trade may be open to debate, it has not prevented a decline in legal alcohol consumption, of more than 20 percent between 2010 and 2016—or around 30 percent on a per capita basis. During that time, tracking system-related costs, as well as tax rises in 2010 and 2013, will have exacerbated the cost differential between stamped products on the one hand and artisanal and smuggled products on the other.

Estimates of recorded and unrecorded alcohol use in Morocco

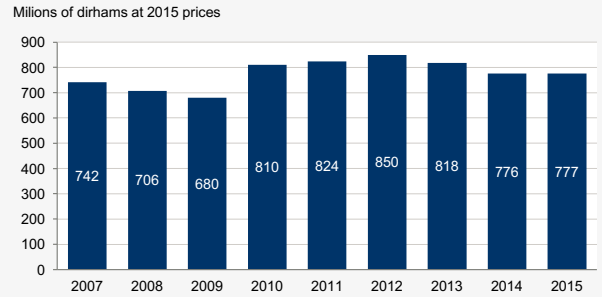


Source: Oxford Economics * OE interpolation of ISWR volume data

3.7.5 Impact on government revenues

Industry sources suggest that the amount of interior consumption tax paid in relation to beer increased by 14 percent in inflation-adjusted terms between 2007 and 2012, but that these revenues fell by nine percent on the same basis over the following three years, as sales volumes for taxed products declined. Partial data also point to a steep drop in tax revenues from wine sales between 2014 and 2015. These sources also suggest that beer- and wine-related tax revenues lost as a result of artisanal and smuggled products may be in the region of 100-200 million dirhams (US$10-20 million). That would be equivalent to broadly 10-20 percent of total Moroccan beer- and wine-related tax receipts.

Inflation-adjusted consumption tax revenues from beer



Source: Indiustry sources; Oxford Economics

[8] See for example Michael Norgrave, The quest for quality data requires hard and radical solutions, WCO News No 75, October 2014, World Customs Organization.

4. Are Tax Stamps Effective?

The preceding case studies suggest that tax stamps play only a limited role in revenue protection and the curbing of illicit trade. Moreover, the studies demonstrate that their efficacy depends on a wider system of regulatory oversight, enforcement and deterrence, and where the tax and regulatory system is not so onerous so as to stifle the operation of legitimate alcohol channels. At worst, tax stamps can lead to unintended consequences by acting as a cover for illicit trade (e.g. through counterfeited stamps or refiled stamped bottles), and/or by exacerbating the price differentials between taxed and informal products.

Of the limited advantages of tax stamps, the case studies highlighted the following:

- As shown in the Turkish example, tax stamps were, albeit briefly, an effective mechanism for reducing illicit activity, by deterring retailers and consumers from purchasing products that do not bear tax stamps.
- As demonstrated in South Korea, more sophisticated implementation has made it more challenging, if not impossible, to counterfeit products. However this is an expensive option that is unlikely to be suitable for high volume or low cost alcohol products.
- Modern tax stamp systems can aid consumer awareness and engagement about quality standards and provenance, as seen in the studies of both South Korea and Turkey, particularly when integrated with mobile application use.
- In addition, the use of tax stamps might be helpful in providing a visible cue to reassure consumers that the government is acting to protect them from health risks from unregulated products.

Despite these benefits, the case studies and wider literature highlight a number of difficulties with tax stamps. These include:

- Before introducing a tax stamp system the authorities should undertake a robust analysis of the size and shape of the illicit market, and assess whether tax stamps will have any impact on the problem. For example, if the illicit problem involves unregistered production that occurs outside the formal supply chain, what impact, if any will the tax stamps have?
- Post implementation assessment should also be part of a tax stamp regime, both to correctly assess the impact, and to identify whether the scheme is operating as envisaged.
- Tax stamp systems will only be effective in combination with robust enforcement mechanisms to identify missing or false stamps, or where consumer awareness (and notification) is sufficient. Often interventions are determined primarily through risk and intelligence; consumers are rarely sufficiently aware or motivated to verify tax stamps and report any concerns.
- Enforcement can also be costly; for some schemes the enforcement authorities need to be equipped with special handheld readers to enable them to detect illegal products. The risk is that this may add to the overall expense of a system that might be passed on to the consumer in higher product prices, fuelling demand for illegal products.
- Rapid advances in technology have meant that tax stamps put in place only a few years ago are quickly susceptible to counterfeiting. Such counterfeiting is known to have taken place in, for example, Turkey (although with the 'new generation' stamps introduced there in 2015, detection of fake stamps has been made easier). This means that regular and sophisticated updates may be needed to secure long-term benefits. Authorities considering the implementation of tax stamps would be well advised to consider this before applying this system.
- Both initial implementation and regular updates can be costly for authorities and manufacturers alike. As shown in the case studies, in each of Turkey, Korea and the UK, significant set-up and ongoing costs have been incurred. Legitimate industry often regard the imposition of tax stamps as an unwelcome additional cost of doing business—especially where the use of a particular stamp is mandated or where a scheme's suppliers determine the cost. The introduction of tax stamps can, for example, mean that businesses must redesign bottling lines, manage the receipt and use of stamps, prepay taxes when buying the stamps and suffer reduced production efficiencies due to the paper and adhesives required. It has been suggested that the additional cost of tax stamps may even act to deter new businesses from entering the legal market.
- There has also been some criticism related to delivery of tax stamp schemes, which are usually subject to a tender process and supplied by an external contractor. Such tender processes take time and government resources to administer and officials may or may not have the necessary skills and experience of tender processes or understanding of the technology behind modern tax stamps. Likewise the rigidity of tender processes can mean that, once a supplier has

been accepted and a contract in place, that particular sort of tax stamp is used for several years in line with the contract, even if it becomes outdated or subject to significant counterfeiting as mentioned above.

- Even if delivery is outsourced, revenue authorities will usually be responsible for controlling both the products and the tax stamps, which takes a significant toll on human and fiscal resources.
- Importantly, tax stamps could ever only ever be part of a broader solution to illicit activity. Their effectiveness can be undermined not just by the particular design or technology but by wider considerations or policies that affect demand. This might, for example, be the robustness of the wider anti-illicit strategy or the relative affordability of taxed and stamped products, as seems to have been the case in Turkey where progress due to stamps was undermined due to large rate hikes that acted to incentivise illicit activity regardless of the tax stamp regime.

5. Alternative or Complementary Measures to Combat Tax Evasion

As we have seen, in many jurisdictions tax stamps have been introduced as a mechanism of revenue control, intended to reduce illicit activity and reduce tax evasion. But as the review has also demonstrated, tax stamps will not work in isolation. In particular, their effectiveness relies on two things—a carefully considered and well-structured wider tax policy; and the existence of a credible and well-resourced information and enforcement regime. Indeed, if the tax is well-designed and enforcement is sufficiently robust, then potentially costly tax stamp schemes could easily be avoided altogether, with little revenue impact. It follows that governments considering introducing a new stamp scheme should examine whether alternative policies could achieve the same aims at a lower cost. Here, we explore the various alternative or complementary measures that could be used instead of or alongside tax stamps.

In terms of wider tax policy, it is possible to establish a set of guiding principles or structural requirements that will help create an environment that encourages tax compliance. Effective responses to tax evasion and illegal trade rely on the establishment of comprehensive cross-cutting strategies to reduce both the supply of and demand for illegal products, and must recognise certain basic determinants of success. For example, it is critical that policy makers implement alcohol tax regimes that are simple to administer, non-discriminatory and impose reasonable tax rates to reduce incentives for illicit trade, protect revenue and encourage responsible drinking decisions for those that choose to drink.

Any system of effective revenue control will also rely on good licencing practice, high quality and timely information capture and well-resourced authorities with appropriate tools at their disposal. For example, an excise operator's license should be a privilege not a right and it is essential that 'rogue' operators are not allowed to enter the trade. This requires a system of strict controls on licencing and the maintenance of a national electronic database of all excise operators that contains risk and compliance data and can be analysed to identify trends across trade segments – for instance, by volume of production or region – and enable resources to be deployed according to compliance risk.

Where possible, integration of excise databases with import and export data should be sought in order to obtain a full picture of the trading activities, as a helpful aid to effective controls. Effective controls also require robust supply chain controls and policy makers should consider licensing of wholesalers and, perhaps, retailers of alcohol beverages plus transporters of alcohol tax free under bond as the most effective system. However, although 'Know Your Supplier/Know Your Customer' like this are certainly good business practice, the licensing of wholesalers and retailers will only be successful if there are sufficient resources to administer and enforce controls on such a large number of traders.

Even where tax stamp systems are implemented, successful anti-fraud strategies also depend heavily on well-designed and well-resourced surveillance, interception and deterrence activities. Enforcement systems should combine thorough audit, credibility controls and unannounced physical checks in order to cover all the possibilities of tax evasion and avoidance. Effective national controls are also usually characterised by a partnership approach across all enforcement agencies nationally and internationally to tackle illegal trade. Likewise the development of a partnership approach with legitimate businesses and trade associations to tackle illegal trade is an integral part of modern revenue controls.

Details on each of these aspects and more are at Annexe B. Further information is available in 'Guidebook to the Successful Introduction of a Specific Excise Tax on Alcohol Beverages' published by the International Tax and Investment Center in 2011.

6. Conclusion

As this review has shown, the effectiveness of any tax stamp system will depend on both the wider anti-illicit strategy as well as the detail of the scheme. The affordability of taxed and stamped products (taking into account the impact on prices of taxes and the cost of the stamping process itself) will also play a central role. Put simply, while tax stamp schemes may be effective as a means of curbing illicit consumption and protecting tax revenues, that will only be the case if effective monitoring, control and enforcement measures are also put in place, and if tax rates and business costs are not so high as to incentivize illicit consumption at the expense of the legitimate industry.

While it is possible for tax stamps to make a positive contribution to the containment of illicit trade in alcohol and associated losses in tax revenues, this is far from guaranteed without considering a multitude of other factors including careful design, implementation and consideration of the specifics of a market and its influences. Overall however, success in curbing illicit trade and ensuring tax compliance will be assisted, and to a large extent facilitated, by the following:

- Ensuring that the excise duty system is well designed – simple, non-discriminatory and set at reasonable levels;
- Setting excise duty rates at a level that means the difference between the cost of taxed and untaxed products does not provide a significant incentive to shift into the informal market;
- A broad strategy to tackle fraud in the industry that includes a robust understanding of the illicit market based on credible and comprehensive data, a well-resourced monitoring and enforcement regime and sufficient penalties to deter the demand for and supply of illegal product; and
- Where tax stamps exists, ensuring that tax stamps are difficult to counterfeit, and that procedures are in place to prevent other potential abuses of the stamp system. This needs to be appropriately balanced so that additional and unnecessary costs from the introduction of tax stamp regimes are minimised as much as possible for legitimate tax-abiding industry players.

Annexe A:
Use of Tax Stamps Globally

Country, implementation date, further information

Albania, October 1995, required for all imported spirits and affixed at source

Azerbaijan, May 1997, required as evidence of duty/tax payment

Belarus, April 1995, required for imported wines and spirits. Fees are discriminatory

Bolivia, Longstanding, required for all alcoholic beverages at no known cost and affixed by importer

Brazil, February 2002, longstanding arrangements for fixture of selos de controle (strips) to alcoholic beverages changed in favour of complex selo application, purchasing, fixing and accounting procedures

Bulgaria, January 1996, required for wines and spirits. May be affixed in-market or at source

Canary Islands (Spain), longstanding, affixed by domestic or overseas producer/bottler or importer

Colombia, longstanding, 2 stamps, (1) dark green Federal Customs strip stamp and (2) each Department's Consumption Tax Stamp that is changed in everything but 'feel' several times a year, are affixed over the closure of all legally imported spirits. Locally bottled Scotch whisky and domestic spirits only require (2)

Côte d'Ivoire, longstanding, either the serial number must be printed on the bottle label or a strip stamp affixed by the exporter must be used. Missing numbers must be accounted for.

Croatia, longstanding, required for imported and locally produced spirits.

Czech Republic, July 2005, required for all spirits in containers of 20cl and above. May be affixed in-market or at source

Egypt, August 1996, required for all imported and locally produced alcoholic beverages as evidence of tax payment. May be affixed in-market or at source

Estonia, October 2006, for alcoholic drinks over 22% vol. in containers of 20cl and above. From 31 January 2010, the requirement was extended to containers of 5cl and above. Stamps may be affixed in an excise warehouse, customs warehouse or site of the registered trader. In the case of imported products stamps may be applied in market or be exported for application at source

Georgia, October 1998, required for all imported and locally produced alcoholic drinks. Must be affixed at source

Guatemala, unknown date, fiscal stamps required at a cost (Quetzal 0.01) and affixed by importer before release from Customs as proof of payment of taxes

Haiti, longstanding, required for imported spirits except liqueurs and affixed by importer at a cost which discriminates against whisky (Gourdes 15) in favour of other spirits (Gourdes 10). Not known if required for domestic spirits

Hungary, December 1993, required for all alcoholic drinks, except those below 5.5% vol in containers less than 33 cl. May be affixed in-market or at source

Italy, longstanding, required for all spirits which comply with the definition in Annex 1 of 110/2008, intermediate products (such as aromatised wines and liqueur wines) and spirit-based or wine-based RTD products but only if they are packaged in pack sizes exceeding 35cl. To be affixed by domestic producer/bottler, producer/bottler in another EU Member State, or importer

Japan, longstanding, serially numbered strip stamps required for all imported alcoholic beverages. Affixed by importer

Kazakhstan, 1996, required for wines and spirits

Kenya, June 2006, required for all imported and locally produced wines and spirits. Unclear whether affixed in market or at source

Kyrgyzstan, January 1996, required for alcoholic drinks

Latvia, June 1995, excise stamps are required for all wines, spirits and spirit-based products greater than 1.2% vol., but not beer. Stamps are not required for products supplied in pack sizes of 10cl or less. May be affixed either at source or in-market after payment of duties and taxes

Lithuania, longstanding, tax stamps (sometimes described as 'label bands', 'model labels', 'import wrappers' or similar) are required for all wines and spirits sold on the Lithuanian market (apart from 'souvenir alcoholic drinks in vials not exceeding 100 millilitres' or sales via duty free shops, diplomatic missions etc.). Introduced in November 1993 and initially only for imported products, but extended to domestic products in 1996. May be affixed by importer or overseas bottler.

Macedonia, December 1997, 'control stickers' required for imported and domestic spirits, as evidence of tax payment. As goods may not be kept under bond for more than 24 hours, it is impractical to affix the stamps to imported goods on arrival. Affixing them at source means that duty/tax must be paid weeks in advance

Malaysia, February 2008, tax stamp and 'security ink' requirement introduced in December 2004 appears to have been superseded by requirement for all imports to go to bonded warehouse, from which importer collects the goods, after completing the necessary documentation, paying duty on those destined for the domestic market, to which a red sticker is affixed, and purchasing green stickers for affixing to duty free goods

Malta, January 2006, all spirits of 25% vol and above in containers of 50cl or more. May be applied by importer or overseas bottler

Mexico, July 1999, revision of Production & Services Tax (IEPS) Law extended requirement for marbetes (stamps) and precintos (ribbons) to be affixed to bottles and bulk containers respectively of both imported and domestic spirits without

the previous preferential option for domestic producers. Affixed at source, failing which by importer prior to removal from Customs or bond. Costs reviewed every six months for inflation, e.g. 24.69 and 90.00 centavos each (initially 2 and 16 centavos respectively) (January 2004)

Moldova, longstanding, strip stamps are required

Montenegro, longstanding, strip stamps are required for imported and locally produced spirits

Morocco, longstanding, affixed by supplier. Since 1962 all imported bottles of whisky with a capacity of 0.75 litres or more have been subject to this requirement which does not apply to other spirits

Myanmar, September 2010, existing requirement for domestic products to carry "tax paid" stickers to be extended to imports

Panama , longstanding, required (no cost) for all liquors and affixed by importer. Difference in size, colour and statement for imported and domestic

Paraguay, January 1993, fiscal stamps required for imported whisky, costings Gs1.00 per bottle, and affixed by importer

Philippines, longstanding, serially numbered strip stamps required for all alcoholic beverages, as evidence of tax payment. Must be affixed at source

Poland, September 1994, longstanding. Required for all alcoholic drinks. Law requires stamps to be affixed at source but it is understood that the authorities may, on a case by case basis, permit stamps to be affixed to small import consignments in bonded warehouses in Poland

Portugal, longstanding, required for imported and domestically produced spirits, including RTDs and wine products. Not required for beer. Stamps must be affixed in a tax warehouse, either by domestic producers or importers. The latter may alternatively send the stamps abroad for application at the time of bottling

Romania, July 1998, for all alcoholic beverages but wines became exempt in 2004. Tax stamps are required for all alcoholic drinks except wines (still & sparkling) and beer. Stamps can be affixed at source (at suppliers facilities), in a tax warehouse in Romania, at the destination place in Romania (by registered consignees) or in a customs warehouse / free zone (by authorised importers)

Russia, 1995, required for all imported and locally produced spirits. State Regulation Law of July 2005 would to have required new form of stamp to be affixed on RF territory; this requirement was opposed. Introduction of new UFAIS software system caused lengthy blockage of imports (winter 2006/7) but requirement to affix the stamps in the RF was either removed from the legislation or subsequently lapsed as, in practice, December 2011, stamps are known to be affixed in private bonded warehouses in e.g. Latvia or at source. There is, however, a proposal to require the affixing to be done at a single government-controlled warehouse

Serbia, August 1997, strip stamps, previously produced by individual companies and affixed in-market, now obtainable from Ministry of Finance and must be affixed at source. Separate types issued for duty/tax-free border shops and the domestic market

Slovakia, April 1995, tax stamps required for all imported and locally produced spirit drinks. Can be affixed by spirits producers, authorised warehouse keepers, registered traders, authorised tax representative and importers

Spain, longstanding, required for all bottled spirits and spirit-based drinks (above 1.5% vol.) but not fortified wines or similar intermediate products. Since 23/06/06, spirits 6% vol. or less and capacity up to 0.5 litres are exempt from the requirement to display a strip stamp. From 01/04/09, bottles of less than 0.1 litres are also exempt, regardless of the strength of the spirit. Affixed by domestic or overseas producer/bottler or importer

Thailand, longstanding, requirement modified during 1992 to make it compulsory for stamps to be affixed at source

Turkey, July 2007, required for all alcoholic beverages

Ukraine , October 1995, required for all imported and locally produced spirits. They must be affixed at source. Later extended to all alcoholic beverages then, in 2010, products not exceeding 8.5% vol. exempted. Issue, resulting in confiscations for non-compliance in October 2011, with excise duty payable at the time of bottling having to be shown on stamp; in some instances products are bottled before stamps are affixed

United Kingdom, October 2006, required on alcoholic drinks of 30% vol and above in containers of 35cl or more. Two formats available, either a circular self-adhesive stamp to be applied to the bottle or a stamp incorporated in bottle labels bearing a trademark

Uruguay, July 1999, requirement for importer to apply for and affix, within set timescale, fiscal stamp (no cost) to whisky imported in bottle extended to all other imported spirits. In October 2005 fiscal stamp required to be affixed also to locally produced/bottled whisky at time of production/separation.

Uzbekistan, October 1996, required for all alcoholic beverages. May be affixed in-market or at source

Venezuela, longstanding, required for all alcoholic beverages: coloured red (Bs43.00 per bottle/strip) and affixed by importer including for Margarita Free Port

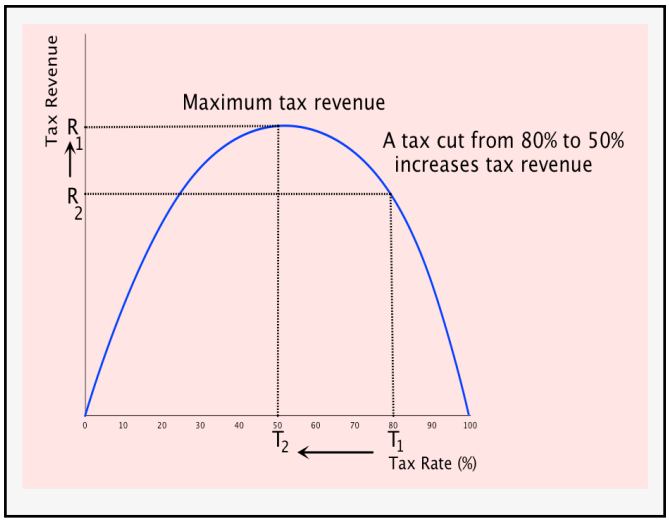
Vietnam, December 1997, special stamps issued by the Customs Bureau must be affixed to all legally imported bottled spirits

Annexe B:
General Principles of Excise Taxation

In line with tobacco, automobiles and other commonly excisable goods, sales of alcoholic beverages have long been subject to excise taxes, as a means for governments to raise revenues. Further information on academic studies of excise taxation and the difference between excise and Value Added Tax is at Annexe C.

Key to successful excise tax policy is the understanding that, while many different methodologies can be adopted, an overall, economically balanced treatment of sales must be achieved if revenues are to be optimized.

This paper describes, and offers case studies to illustrate, many of the different options available. However, for a clear introduction and insight into the question of optimum balance, a rewarding starting point is an understanding of the 'Laffer Curve' general principle, and of the effect of taxes on consumer prices.



If excise tax rates are set too low, and consumer prices stay relatively cheap, then a government will not realise as much revenue as it could. This is an incentive to set higher rates. But if rates are set too high, then consumer prices will also rise too high; the products will become unaffordable, and the government's revenue will also be lower than it could be, as sales volumes fall.

The 'sweet spot' on the Laffer Curve is at the top of the bell curve, where the rates are set at a reasonable level, allowing sales to consumers at a reasonably affordable price, resulting in the right volume of sales to generate optimum excise revenues.

In addition to sub-optimal revenue, setting excise rates too high can also result in other, perhaps unexpected and unintended, economic and social consequences. It is often observed that, in countries where high rates of duty are set, there is often a greater incidence of smuggling (further reducing revenues), and tax evasion such as non-declared domestic production. Counterfeit goods and use of illicit goods (which in the case of alcohol can be hazardous to public health) also tend to increase in higher-rate environments.

Setting tax rates at a high level does not take into account the impact of availability of cheap illegal products. Where excise controls on domestic production and smuggling are not effective, consumers with limited funds available often choose to purchase cheap illegal products rather than deprive themselves of other goods in order to purchase the tax paid alcohol. Excise taxes are regressive in that they bear most heavily on the poorest members of society. Studies in the UK and USA have shown that the key consumers of illegal alcohol products are those who come from the lowest income group.

The government will want to set a tax rate that will generate maximum revenue but not be so high as to create demand for illegal products, incentivise tax evasion or smuggling or force consumers to trade down or change their consumption patterns (particularly relevant for 'ad valorem' excise tax regimes).

Only those countries with extremely effective revenue and customs authorities operating robust strategic approaches to tackling illegal trade in alcohol beverages are able to impose high rates of excise tax without suffering illegal trade in excess of 20 percent of consumption.

Countries with a long history of excise duties tend to have an excise tax structure based on the alcoholic strength of the product. Countries that have decided to introduce excise taxes to compensate for reducing customs duties have often adopted an 'ad valorem' structure for the tax basing the tax rate on the value of the goods. Some countries have a hybrid structure.

The specific structure is recognised as being easiest to administer and control with a small taxpayer base of manufacturers and importers of alcohol products and bonded warehouse keepers. Usually, duty is charged on release of the products to the domestic market. Many countries allow manufacturers and owners of the products to store goods tax-free in bonded warehouses until the goods are delivered to the domestic market. Because the rate of tax is based on strength of alcohol, there can be no disputes or fraud associated with the value of the goods. It is therefore easy to calculate. Importantly, credibility controls can be operated to ensure that declarations of production match the inputs to the production process. To ensure that a specific tax on products keeps pace with inflation regular but minimal uplifts of the tax rate could be considered.

The 'ad valorem' structure is based on the value of the goods. This structure is much more difficult to administer and control as valuation can be easily understated. Administration becomes even more difficult where the 'ad valorem' excise rate structure is combined with a transaction tax process structure. This extends the taxpayer base to wholesalers and retailers and simultaneously extending the opportunities for fraud exponentially.

Advocates of the 'ad valorem' structure consider that, because it favours the lower priced products, people on limited incomes are less likely to move to the illegal market under this system. Also, an 'ad valorem' structure will naturally keep pace with inflation and does not require regular uplifts in tax rates.

ANNEXE C:
Academic Studies of Excise Taxation and the Difference between Excise and Value Added Tax (VAT)

Cnossen[9] defines excise taxation as selective in coverage, discriminatory in intent and often some form of quantitative measurement in determining tax liability. This contrasts with general consumption taxes such as VATs and retail sales taxes that are defined to include all goods and services for sale in the country other than those specifically exempted. Control of excise taxes is usually through physical as well as audit controls. There are also major differences in the number of taxpayers involved with excise, typically, confined to a small number of licensed or authorized producers and warehouse keepers who have to lodge significant financial securities for the privilege of being allowed to operate on excisable goods tax free. Excise tax is usually charged when the excise goods leave the bonded premises for the domestic market. This small tightly controlled taxpayer base makes excise taxes the most efficient to collect provided that good audit and physical controls are in place to prevent undeclared production leaking into the domestic market.

VAT, on the other hand, is based on collecting comparatively small amounts of "value-added" at each stage of the supply chain and therefore involves a large number of taxpayers at the production, wholesale and retail levels. Because tax is charged only on "value-added" and is usually a small percentage (5 percent to 25 percent) in comparison with excise taxes (sometimes 70 percent or more of the retail selling price), the revenue at risk is deemed to be less for each taxpayer. VAT is usually charged on top of any excise duties so if excise duties are evaded VAT is evaded too.

Economic theories developed during the 20th century have included the proposal that tax rates should be determined according to the theory of elasticity of demand (Ramsay 1927). The absence of close substitutes for addictive or indispensable products, such as tobacco, alcohol and energy, implies that the demand for them is inelastic and the theory prescribes that as long as goods are unrelated in consumption, the tax rates should be higher on those with the lowest elasticity.

There have been many subsequent studies of different aspects of the relationship between price elasticity of demand for a potentially addictive commodity of which the most influential have been those by Becker and Murphy in 1988, Kenkel in 1993, Manning, Blumberg and Moulton in 1995 and Grossmand, Chaloupka and Sirtalan in 1998. Another key influence on considerations about setting the appropriate tax rate has been the Laffer curve, the representation of the relationship between rates of taxation and the resulting levels of government revenue, named after Dr. Laffer in 1978, which we introduced at the top of this paper.

Excises have also been rationalized as charges for the external cost (e.g. in healthcare, dealing with drink-related crime etc.) that consumers or producers of excisable goods impose on others (Pigou 1918). Thus, the expectation would be for the tax rate to be equal to the costs of drink-related harm to society.

[9] Professor Sijbren Cnossen "Economics and Politics of Excise Taxation" 2005 - http://oxfordindex.oup.com/view/10.1093/0199278598.003.0001

ANNEXE D:
Effective Revenue Controls on Production/Operation on Goods or Storage of Alcohol Beverages Under Bond

1. A small number of taxpayers paying large amounts of duty/tax

Set the tax point at production, operations and initial storage payment makes for the smallest number of taxpayers to control. Tight regulations can be set and privileges granted in terms of authorisation of warehousing facilities tax-free under bond and movement of goods between authorised facilities tax-free under bond.

2. Require financial security to cover duty/tax at stake

Two sorts of financial security or bond are required. The amount of financial security needs to reflect both the compliance history (with all tax and other government regulations) of the trader and the value of excise duty (and VAT) at stake say, over the course of a month (for production or storage premises) or for a week's deliveries (for the movement guarantees). The level of guarantees should be set by reference to stocks and deliveries over the previous 12 months. A movement guarantee may be provided by a licensed transporter or by the purchaser rather than by the vendor of the goods. Very large operators with good compliance history may be allowed to hold a lower level of financial security for both the premises and movements guarantees.

3. Licence only "Fit and Proper Persons" as excise producers, importers and warehouse keepers

The ability to produce, operate on and store alcohol beverage products without payment of duty/tax should be regarded as a privilege not a right. Licences should only be granted to traders who can satisfy the Revenue Authority that they are "fit and proper persons". Each applicant for a license should undergo a risk assessment based on his/her compliance history as a taxpayer and law abiding citizen. A criminal record or evidence of connections with criminal organizations, debt, bankruptcy, fraud or non-compliance with legislation (including, for example, health and safety, employment and environmental legislation) should be reason to deny a license or approval. Revenue authorities may wish to restrict taxpayers by requiring a separate license for each set of premises where alcohol is produced or where operations on bonded goods take place. Legislation can then provide for anyone found to be producing, storing, bottling or transporting commercial quantities of alcohol without a valid license to be committing an illegal act. Licences should be numbered, displayed prominently at the principal place of business, quoted on commercial documentation and reviewed annually.

To assist in controlling the manufacture and distribution of bonded goods, revenue authorities may require that licensed persons seek approval of premises and operations, accounting and record-keeping systems and distribution vehicles and operators before production, storage or operations may commence legally. These can be important tools in revenue control as revocation, short-term suspension or variation in the operations approved can be very effective sanctions on a business.

4. Maintain one national electronic register of licensed excise taxpayers

The Revenue Authority should maintain one national electronic register of all taxpayers holding excise licences. Unlike a Value Added Tax where anyone trading over the registration threshold limit cannot be refused registration, the Revenue Authority can refuse an application for an excise license. Where a license has been refused a record should be kept on the national register to ensure that subsequent attempts by the same taxpayer (or by associates) are easily identifiable. The national register brings together all essential details about the taxpayer including return and payment details as well as information about any minor contraventions. This information can be used to inform risk assessment and determine the allocation of resources for control. Because of the high value of excise tax involved, it is important to ensure that all official actions are recorded and auditable and available for inspection by a separate, remotely located team of officials at regular intervals to guard against corruption.

Finally, an up-to-date electronic national register of all operators licensed to produce, operate on, store or move alcohol beverages tax free under bond is essential to facilitate quick and easy references to other revenue/customs authorities under Mutual Assistance Agreements.

5. Audit and Credibility Controls

Controls need to be based both on systems-based audit (including audit of computerised systems), individual transaction checks and on physical checks of the premises to ensure that (for producers) all the pipework and valves are as declared on the production process diagrams provided at licensing/authorisation, that all VATs and containers have been measured regularly by an objective external (usually public sector) authority, that full security and management controls are in place (see Annexe B).

One of the key features of excise controls is the constant need to assess what is happening at the production/operation/storage premises with declarations. It is useful to require electronic returns of production including details of the key inputs and monthly stock records showing receipts and movements out (to the domestic market on payment of duty or to another licensed operator or premises under bond or to export) for individual transaction checks through the financial and commercial records and for checks with the loading details of transporters.

Overall production declarations can then be compared with the expected results based on inputs (raw ingredients, bottles, closures, labels, machinery records). Companies usually try to maximise the production from the ingredients so as to maximise profits and there is usually a consistent scientific relationship between ingredients and product produced. These results can be compared (using analysis of the national register data) across all producers of similar products to identify those who might be concealing production and therefore worthy of closer investigation.

Putting together information from the monthly stock records, imports and exports for each excise trader provides a useful indication of the overall picture of the way in which the business is trading. Again, comparisons can be made across producers of the same or similar products, in the same region and of a similar size to identify any unusual patterns.

Allowances are usually given for wastage and again this can be a scientifically calculated amount. Accidental breakages/ losses need to be reported to the Revenue Authority for checking. Accidents reported in transport need to be backed up by a police report and/or insurance claim.

Where credibility checks reveal potential differences between declarations and calculated production officials should be able to issue an assessment calling for the additional duty due. The trader then has to prove that his/her declaration was accurate or pay the additional amount. Before any such assessment is issued the official (s) concerned should expect to have to convince a remote manager of the validity of their argument in order to minimise corrupt practices.

Audit checks must also cover the financial records for all transactions involved in purchases and sales, payments to third parties e.g. for transport, security or machinery maintenance services and to identify under or over-invoicing of international supplies by multinational companies. Audit also needs to include an interface with the Import/Export and VAT declarations for the business. Specialist audit skills may be needed to examine electronic accounts and records.

6. Powers of revenue officials

Officials should have powers to enter and inspect licensed or approved premises at any time without advance notice. The powers should provide for officials to seize any equipment, goods or records as required for investigation. Operations on and movements of undeclared production are likely to occur under cover of darkness and outside normal revenue officials' working hours. It is important to ensure that budgets and terms and conditions of employment of officials cater for unannounced visits to all licensed excise premises at a frequency determined by risk assessment.

Where there is evidence of unrecorded production and/ or deliveries of alcohol beverages without proper payment of tax, powers should enable officials to close the premises and stop further production or movement of products whilst investigations take place.

7. Supply Chain Controls for onward movements under bond

Supply chain (or distribution) controls are critical for ensuring collection of the full tax owed and must be legally enforceable. Equally important, such controls must be in place to ensure that the products are both authentic and safe.

Most countries allow specified operations involving alcohol beverages and storage of finished product under bond in approved tax warehouses. All licenced excise traders should be required to check the validity of anyone to whom they sell or send bonded goods, and implement and maintain robust internal security controls. All excise traders must provide evidence of removals of goods and receipts of goods whilst they are under bond. When goods leave the bond to enter commerce tax must be accounted for.

Many countries require that warehouse keepers and owners of alcohol beverages under bond may use only transporters licensed specially by the Revenue Authority to move alcohol products under bond. All documentation must carry details of the licensed transporter used. Licensing the transporters provides a legal obligation for the transporter to comply with revenue requirements including on the spot inspection of vehicles and documentation with the power to issue civil penalties, suspend transport activities for a period or take criminal action.

In this way, all goods moving within the legitimate supply chain (assuming it is limited to production, operations and initial storage before supply to wholesale or retail) can be accounted for. Anything not accounted for is treated as illegal and the taxpayer penalised accordingly.

Although several countries have had a requirement for bottles of spirits sold for consumption domestically to bear a simple form of paper tax stamp, the interventions that have been most successful in countering smuggling have come from intelligence and risk assessment not from the tax stamps. Track and trace technology has advanced dramatically over recent years and many authorities are now exploring the use of technology for track and trace of alcohol products as another tool in the fight against illegal trade.

8. Supply chain controls – purchases

Recently, in an effort to reduce illegal trade, some of the largest alcohol producers have tightened their purchasing procedures to ensure that they take 'due diligence' measures in their dealings with suppliers. This usually entails contractual agreements that specify that the supplier must not knowingly supply goods or services used in the production or in operation on alcohol beverages to any customer who is not a licensed or approved alcohol producer or warehouse keeper and must not sell goods or services for cash, including sales for export. Whilst not a complete safeguard against suppliers also making their goods or services available for illegal purposes, such purchasing agreements serve to reinforce the ethical standards expected in well run businesses and provide a rationale for alcohol producers and warehouse keepers to refuse to do business with suppliers if they are not satisfied with the integrity displayed.

The supply chain control practices outlined should be expected/required by revenue authorities as part of the license/approval conditions.

9. Memoranda of understanding or agreement

A useful tool in cementing a partnership approach between the Revenue Authority and Trade Associations representing the different segments of the alcohol industry can be standard Memoranda of Understanding or Agreement. An example from the UK is at Annexe C.

10. Licensing wholesalers and retailers to deal in alcohol beverages

Governments may decide to extend supply chain controls by requiring all wholesalers and retailers dealing in alcohol beverages to be licensed. Part of the requirements under such a licensing regime would be the need to comply with certain standards e.g. for record-keeping, not accepting cash

purchases (for wholesalers). The license may combine the requirement for the operator not to sell alcohol beverages to customers who are under the legal age limit for alcohol consumption. Difficulty with implementing such requirements lies with the very large number of wholesalers and retailers who would need to be under revenue authority controls and the resource and cost implications and, for this reason, such licensing requirements have rarely been introduced. An alternative in some countries is for the state to hold a monopoly on retail sales e.g. Systembolaget in Sweden.

Without special revenue authority licensing it is still feasible to introduce appropriate penalties to deter wholesalers and retailers from purchasing illegal goods and these provisions can be used to good effect when intelligence or investigations reveal that illegal goods have been sold to consumers through a wholesale or retail outlet.

11. Reducing Demand

Without demand there would be no market for illegal products. Demand results from consumers wanting to have potentially addictive alcohol products and preferring to purchase cheap untaxed alcohol beverages. Often they are not aware of the potential dangers of consuming counterfeit or adulterated products though the cheap price and purchases made through friends and acquaintances rather than through a recognised retail outlet should provide a signal. Sometimes, retail outlets supply both taxed and untaxed goods depending on how well the retailer knows the customer. Here, customers having a long relationship with the retailer are likely to trust that the "cheap" supplies are "special offers/bargains" without realising that they are being duped with goods that may be extremely detrimental to their health.

In the UK, the Department of Health has been working with HM Revenue and Customs over several years to warn parents, in particular, of the dangers of their children being offered illegal cigarettes. The campaign – known as "Keep It Out" has had modest success in raising awareness of illegal trade and in reducing illegal consumption. Consideration is now being given to adopting a similar campaign to warn adults and schoolchildren about the dangers to health of consuming illegal alcohol.

12. Strategic Approach to Tackling Illegal Trade – tackling supply and demand

Following on from the advent of the EU Single Market in 1992 the significant increase in alcohol fraud identified in the UK's Alcohol and Tobacco Fraud Review of 1997 led to the development of a comprehensive strategic approach to tackling illegal trade – both undeclared domestic production and smuggling. Whilst the UK revenue controls on production of alcohol can be considered to be among the best in the world, there is significant fraud from smuggling or diversion under the EU excise movement and control procedure.

The combination of national collaboration across the public and private sector including working with the Department of Health to tackle demand and with the Local Authorities to tackle distribution at the retail level plus international collaboration across enforcement agencies has proved to be the most effective way to keep illegal trade in alcohol products to an acceptable level in the UK.

There have been several iterations of the UK's Alcohol Strategy culminating in the 2016 Alcohol Strategy see - https://www.gov.uk/government/publications/hmrc-alcohol-strategy. A key part of the strategy is the strengthened partnership between the HM Revenue and Customs and the industry through a Task Force Working Group to focus on minimising illegal trade in alcohol beverages. Their 2015 report is at: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/448659/04818_JAAT_Annual_report_2015.pdf.