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Tobacco Control: Interviews and Articles, 2015-2016

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Robert Ireland

Abstract

This WCO document includes a compilation of previously published tobacco control interviews and articles from the period of 2015-2016. Sub-topics include tobacco taxation, plain packaging, illicit trade, and Investor-State Dispute Settlement (ISDS) mechanisms.

Key words

Tobacco control, tobacco taxation, plain packaging, illicit trade, ISDS

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Interview of Harry Clarke and David Prentice, researchers from La Trobe University's School of Economics, Melbourne, Australia by Robert Ireland, Head of WCO Research Unit

Cigarette smoking is an activity that directly leads to significant health problems, such as lung cancer. The World Health Organization (WHO) estimates that tobacco kills up to half of its users, and nearly six million people each year. The trade in tobacco is also a concern for Customs administrations, particularly aspects related to tax evasion and counterfeiting.

A recent development in tobacco health regulations is the introduction of 'plain packaging' (PP) of cigarettes, which requires the removal of all branding except for the brand name in a mandated size, font, colour, and location on the pack. In 2011, the Australian Government passed the Tobacco Plain Packaging Act, becoming the first country requiring tobacco products to be sold in PP. Ireland and the United Kingdom (UK) are currently considering PP legislation too. An interesting question for Customs is whether PP will affect the level of tobacco smuggling and revenue collection.

Economists Harry Clarke and David Prentice from La Trobe University's School of Economics in Melbourne, Australia, published a paper presenting their empirical research on PP and its implications, including the overriding issue of public health, but also the sale of illegal cigarettes: Clarke, H. and Prentice, D. (2012), Will Plain Packaging Reduce Cigarette Consumption?, *Economic Papers: A journal of applied economics and policy* 31: 303–317.

Robert Ireland, the WCO Head of Research and Communications, conducted the following written interview with Dr Clarke and Dr Prentice.

What are the main purposes of tobacco PP?

The main purpose of legislating tobacco to be sold in PP is to discourage smoking and, in particular, to discourage young people from taking up smoking. This is done by removing what was, in Australia, the last form of advertising of tobacco products, namely its packaging. It is important to note four features of the Australian cigarette market that motivated the legislation as, in effect, almost all other major policies available to discourage smoking have now been implemented:

- First, cigarette smoking is now largely concentrated among three groups within Australian society: indigenous Australians; migrants from certain countries, and less-educated Australians working in low-prestige occupations;
- Second, all other forms of advertising by manufacturers and retailers are now prohibited, and there are restrictions on smoking at work and in other public places;
- Third, cigarettes are heavily taxed;
- Fourth, almost all smokers begin when they are young.

Hence, restricting packaging, in conjunction with other measures described below, appears to be almost the last regulatory intervention, short of prohibition, available to discourage smoking among these groups that have continued smoking.

Could you summarize the main components of Australia's PP legislation?

The *Tobacco Plain Packaging Act* took effect on 1 December 2012. Its main components are: to make it an offence to sell tobacco products not in plain packaging; to require packaging to be a standardized, featureless (except for prominent graphic health warnings), drab dark-brown with the font for the brand name also standardized, and cigarette sticks standardized without trademarks, etc.; and to impose penalties for non-compliance of 220,000 Australian dollars for individuals and 1.1 million dollars for corporations.

The legislation was also accompanied by three sets of complementary policies: a large increase in the excise on tobacco in April 2010; negative advertising campaigns, both general and targeted (at groups like indigenous Australians, for instance); more extensive inclusion of anti-smoking treatments, such as nicotine replacement therapies, under Australia's Pharmaceutical Benefits Scheme, making them more accessible. Since then there have been further tax increases.

What were the questions you investigated, and the main findings of your paper on PP?

Our paper set out to do two things. First, to provide an economist's review of the legislation and its policy context. Second, to empirically analyse one of the main criticisms of PP, namely the tobacco industry argument that PP might actually increase quantities of cigarettes demanded because it would induce lower prices. This was claimed to be plausible because, with more standardized packaging, PP would increase competition among existing manufacturers, from new firms, and from illegal unbranded and counterfeit cigarettes.

Our analysis was conducted using Australian data on cigarette prices, brand numbers, and market shares following two earlier episodes of increased restrictions on advertising. These were, respectively, the restrictions on electronic advertising in the mid-1970s, and restrictions on print advertising in the early 1990s.

The research showed that there was evidence of price-cutting following each of the earlier advertising restrictions. This took the form of quantity discounting with firms offering larger numbers of cigarettes per pack with a lower per stick price. However, there was no evidence of competitive entry or of substantial changes in the supply of illegal cigarettes.

There has been no substantial legal entry into Australia since the early 1970s and, not long after print advertising was prohibited in the early 1990s, the cigarette companies almost completely ceased introducing new brands. This is consistent with advertising restrictions increasing price competition and making the market less profitable. Less profitable markets are less likely to see entry – legal or otherwise.

Our results suggest that, introducing PP will be followed by some price-cutting. This can readily be addressed by increasing cigarette excises. But, importantly, our results also suggest that it is highly unlikely that there will be entry by new competitors or a substantial increase in the supply of illegal cigarettes.

What is the likely impact of the PP law on counterfeit and illegal unbranded cigarettes in Australia?

The PP law is unlikely to have a substantial effect on the market for counterfeit and illegal unbranded cigarettes for three reasons:

- First, although removing the packaging of legal brands will make illegal cigarette brands relatively more attractive, this will be offset to some degree by the lower prices of the legal brands, resulting from greater price competition among them;
- Second, the cost of supplying illegal unbranded cigarettes has increased and will continue to increase post PP. The cheapest source of tobacco for illegal cigarettes used to be those supplies diverted from the legal domestic production of tobacco. However, it has been illegal to grow tobacco in Australia since 2006 and so tobacco for illegal cigarette production either has to be produced illegally itself or imported. Both of these activities are costly;
- Third, tobacco is bulky and relatively low value compared with other illegal imports, and Australia's borders are relatively easy to police compared with other countries.

Following PP, the cost of supplying imported illegal cigarettes to Australia will increase further as manufacturers have to produce them specifically for Australia, rather than coming from larger production runs for multiple countries. Anecdotes in a Deloitte 2011 report prepared for the tobacco industry are consistent with illegal manufacturers not making Australia-specific packages before PP as they omitted the health warnings.

The three largest Australian cigarette firms funded a 2011 study by Deloitte that claimed the share of illegal cigarettes in Australia is significant and increasing – 6% of cigarette sales in the country in 2007, and 15.9% in 2010. Based on your research, what conclusions did you reach about these aspects of the Deloitte study?

Our analysis of Euromonitor (an independent company that specializes in strategy research on consumer markets) data on brand market shares suggests that there was no substantial increase in the share of illegal cigarettes between 2005 and 2010. If there had been a large increase in the share of illegal cigarettes, it is likely that there would have been changes in the market shares of the large market-share brands.

Even though we cannot observe the market share of illegal cigarettes, large changes in their demand will affect the sales, and therefore market shares, of individual brands differently. This is because illegal cigarettes are more likely to take market share from some brands (probably discount brands) than others (premium brands).

A somewhat analogous situation occurred when the discount legal brands were introduced from the late 1970s. This was followed by large changes in the market shares of existing large brands. However, on examining Euromonitor's data between 2005 and 2010, the market shares for existing large brands are extremely stable. This suggests that there has been no large change in the share of illegal cigarettes.

We note that Ireland and the UK are considering legislation similar to that adopted in Australia. Do you think the findings of your research are generalizable to other countries that are considering PP laws?

The main results of our work will be largely generalizable to Ireland and the UK. This is because our results are consistent with features of the cigarette market that are common to any market for a differentiated product. Removing advertising reduces differentiation and increases price competition. However, greater price competition also makes a market less profitable, which means entry by new firms and the introduction of new brands are less likely. Furthermore, PP also discourages the importing of illegal cigarettes by raising the costs of doing so, and reducing the profit margin.

One potential difference is that Ireland and the UK's proximity to the rest of Europe make it likely that competition from illegal cigarettes will be a greater problem with PP. Indeed, illegal sales in the UK via illegal imports and counterfeiting legally produced brands exceed 10% of total sales. There are several points here. It might be necessary to intensify efforts to restrict smuggling, and to make it more difficult to reproduce standardized PP packaging – which can be “aversive” but still difficult to duplicate.

As remarked above, these difficulties can be exaggerated. Their illegality places a natural cap on their share, as the larger the market share the easier it is to detect and punish illegal cigarette importers. Of course, the best long-term defence against illegal imports is to encourage high taxes and PP in other European countries.

Are there any updates you would like to share since the publication of your 2012 paper?

A major issue that has become clear both before and after the introduction of PP in Australia has been the sustained campaign of negative publicity launched by tobacco companies to discredit PP policies, both prior to and after PP implementation. This is particularly likely in the UK given the influential role that successful PP laws in the country might have in spawning the same types of policies in other European countries.

This tobacco company campaign in Australia included disinformation often derived from industry-funded data sources, about the effects of PP on legal sales, on the livelihood of small retailers, and even the (false) claim that in Australia PP increased legal tobacco sales because prices fell. Policymakers need to anticipate such responses by having reliable, accurate statistical data available to them, and by arguing clearly prior to policy implementation that PP is a long-term policy that seeks long-term reductions in the prevalence of smoking, particularly among young people.

Any available idiosyncratic short-term data trends will be exploited by tobacco companies to create public opposition to PP. As mentioned too, if greater competition does reduce prices then tobacco excises should be increased.

More information

<http://onlinelibrary.wiley.com/doi/10.1111/j.1759-3441.2012.00186.x/abstract>

Dr Harry Clarke is a Professor of Economics at La Trobe University in Melbourne, Australia. He obtained his PhD from the Australian National University. His current research work concerns resource and environmental economics, and the economics of global climate change. Dr Clarke has authored over 100 scientific publications and two books.

Dr David Prentice is an Associate Professor of Economics at the University of Nottingham's Malaysian Campus. He obtained his PhD from Yale University. His current research focuses on the development of the American Portland and natural cement industries, and pricing and mergers in differentiated products markets. Dr Prentice has published extensively in numerous journals.

Interview of Luk Joossens, Belgian Foundation Against Cancer and Association of European Cancer Leagues by Robert Ireland, Head of WCO Research Unit

The taxation of tobacco is a core policy mechanism for reducing cigarette smoking. Evidence shows that the greater the tobacco tax increase, the lower the cigarette consumption. National revenue agencies, such as Customs, collect enormous amounts of cigarette taxes every year through import duties, value-added tax (VAT) and excise taxes. These taxes fund vital government services.

Estimates of the quantity of revenue collected from tobacco taxes for the five members of the United Nations Security Council alone in 2011 was over 60 billion US dollars according to data from the World Health Organization (WHO): United States (US) – 33.28 billion; France – 14.87 billion; United Kingdom (UK) – 14.07 billion; Russian Federation – 2.41 billion; and China – 0.54 billion (based on currency conversions carried out in April 2015).

The illicit trade in tobacco can negatively impact efforts to reduce smoking because it can lower the price of cigarettes. Accordingly, the causes of illicit trade and the available policy options are of great interest to policymakers. Obtaining data and scientifically measuring illicit trade is challenging as there can be various contributing factors. Moreover, smugglers and counterfeiters do not supply researchers with data.

Extensive peer-reviewed research has shown that taxation is not the primary contributor to the illicit trade in tobacco. Indeed, many countries with high cigarette taxes have low illicit trade rates – for example, Sweden and the UK – while many countries with low cigarette taxes have high illicit trade rates.

Luk Joossens from the Belgian Foundation against Cancer and the Association of European Cancer Leagues, based in Brussels, Belgium, is an international expert on tobacco control who has advised, among others, the World Bank, the European Commission and the WHO. Robert Ireland, the WCO Head of Research and Communications, conducted the following written interview with Mr. Joossens.

What is your analysis of the main causes of the illicit tobacco trade?

Illicit trade is the outcome of classic demand and supply: demand by smokers for cheaper or specific tobacco products, which are perceived as better quality and not available on the domestic market, and supply by legal and illegal tobacco manufacturers looking for more profit, more sales, and increased market shares, or to penetrate new markets, facilitated by corruption, the presence of criminal networks, and weak government enforcement capacity.

Smokers' use of illicit tobacco is related to price and availability. The demand for illicit tobacco products is strongly influenced by reduced prices, often 30% to 50% cheaper than legal products. In addition, supplying the illicit market is attractive to companies and traders because of the low cost of manufacturing – as low as five US cents a pack in Paraguay – and the potential gains to be made when selling products without paying any tax.

It is crucial to note, however, that the solution to this problem is not to lower tax levels. Although a high tax margin may provide the initial incentive to smuggle, data shows that

it is not the only factor. Other important factors include the ease and cost of operating in a country, industry participation, how well crime networks are organized, the likelihood of being caught, the punishment if caught, corruption levels and so on.

Estimates of the illicit trade from 84 countries in 2007 have shown that the proportion of illicit trade in the cigarette market is lower overall in high-income countries than in low-income countries. Corruption has been shown to be a strong predictor of levels of tobacco smuggling, with inadequate laws and law enforcement as well as geography also playing a role. Price levels do not predict levels of illicit trade.

What policy options for reducing the illicit tobacco trade do you recommend?

Combating smuggling is creating obstacles for illicit traders. The incentive for traders is the financial gain; the disincentive is the range of obstacles to making these gains. A mix of policies should be recommended to achieve this goal. In the UK, the gains are high, but so too is the number of obstacles. Cigarette prices in the UK are among the highest in the world, but the illicit cigarette market was reduced from 21% in 2000 to 9% in 2012.

The UK strategy included a wide range of measures designed to curb illicit trade such as the deployment of additional Customs officers, specialist investigators and intelligence staff, more X-ray scanners, tougher sanctions and penalties, a public awareness campaign, supply chain legislation, confiscation of proceeds and international cooperation using overseas intelligence officers.

The global scope and multifaceted nature of the illicit tobacco trade requires a coordinated international response and improved global regulation of the legal tobacco trade. Countries should be encouraged to ratify the Protocol to Eliminate the Illicit Trade in Tobacco Products (ITP). The ITP has been negotiated as a supplementary treaty to the WHO Framework Convention for Tobacco Control (FCTC).

The ITP has three parts: measures to control the supply chain, to improve law enforcement and to enhance international cooperation. Adopted in November 2012, it will enter into force on the 90th day following the 40th ratification of the Protocol. So far, 54 Parties to the WHO FCTC have signed the Protocol, and seven countries have ratified it.

Counterfeit cigarettes are one component of the illicit trade in tobacco. Are these cigarettes more dangerous to smoke than genuine cigarettes?

Counterfeit cigarettes are not a standard and uniform product. They do not respect specific rules or obey regulations. Some counterfeits are made of 'good quality tobacco' and some may include musty raw tobacco processed with sulphur and carbamide to look better. Focusing on the hazardous chemicals in counterfeit cigarettes may result in 'regular' cigarettes being seen as safe, even though they kill half of all regular users, contain 70 carcinogenic chemicals, and are responsible for 6 million premature deaths each year.

Both genuine and counterfeit cigarettes are extremely toxic products. There are no safe cigarettes and there is no safe level of smoking. For instance, in 1989, the US Surgeon General's report listed just a few of the elements people typically consume when smoking genuine cigarettes: carbon monoxide, tar, argon, nicotine, methane,

acetaldehyde, acetic acid, hydrogen cyanide, formic acid, isoprene, nitrogen oxides, phenols, ethylene, acrylonitrile, glycerol, acrolein, ammonia, formaldehyde, benzene, acetylene, styrene, tobacco-specific nitrosamines, anthracene, arsenic, cadmium, chrysene, benzopyrene, vinyl chloride, and radioactive polonium.

Ireland and the UK have joined Australia in adopting laws on plain (standardized) packaging of cigarettes, and France is in the process of doing so. The WHO has stated that “the implementation of standardized tobacco product packaging represents a legitimate and effective tobacco control measure” and “is in accordance with international legal obligations under the WHO FCTC.” As other countries consider similar legislation, it is an important subject for Customs’ cognizance, especially any impact on revenue collection and illicit trade. What are your thoughts?

Tobacco companies have argued that standardized packaging will result in falling prices that in turn will increase the consumption of tobacco. However, evidence from Australia does not show falling prices; rather, price rises have continued over and above tax increases. There is some evidence of trading down towards cheaper brands, but this appears to be a continuation of an ongoing market trend.

Plain packaging was introduced in Australia in December 2012. In 2012, the market share for premium cigarette brands in Australia was 16.9% and in March 2014, after a major tax hike in 2013, 15.1%. This is not a dramatic shift. In many high-tax cigarette countries, value packs become more popular and premium brands lose market share.

Tobacco companies have claimed that plain packaging would result in more illicit trade, because copying and counterfeiting would be easier. Again, the evidence so far shows that the percentage of smokers using unbranded ‘chop-chop’ tobacco remains at very low levels – only 0.2% regular use by smokers in 2014 – and that an increase in the counterfeit trade never happened.

In November 2013 the UK Government commissioned an independent review led by Sir Cyril Chantler into the public health effects of standardized packaging of tobacco. The review stated that they had “seen no convincing evidence to suggest that standardized packaging would increase the illicit market.” Chantler noted that in Australia “hardly any counterfeit standardized packages have been found to date.” Furthermore, a representative of one of the Australian tobacco manufacturers informed Sir Cyril’s team that his company had seen a reduction in counterfeit products following the introduction of standardized packaging in that country.

In addition, in its 2013-2014 annual report, Australian Customs and Border Protection reported decreases from 2012-13 to 2013-14 in several illicit cigarette trade indicators: level of tobacco seized – down from 183 to 178 tonnes; number of cigarettes seized – down from 200 to 147 million sticks; and duty evaded – down from 151 to 139 million Australian dollars.

What does your analysis reflect about the impact of plain packaging of cigarettes?

So far, the Australian experience is a success story. The main objective was to make tobacco products less attractive and it worked. For instance, school-based surveys of students aged 12-17 in 2011 and 2013 in Australia show that the removal of branding and the uniformity of the pack appearance have increased negative pack ratings and

decreased positive ones. As result of a comprehensive tobacco control policy, daily smoking decreased from 15.1% in 2010 to 12.8% in 2013. There was no price war, and no collapse of prices, no loss of market share for small shops, no increase in unbranded illicit tobacco, and even a decrease in cigarette counterfeiting.

The possibility exists that plain packaging might increase price competition between tobacco sellers, leading to lower prices. What should governments do in such situations, if anything?

A price war cannot be ruled out, because it is the responsibility of tobacco companies to set prices. If tobacco companies want to launch a price war, nobody can prevent them. In many countries, the government cannot regulate prices, but can increase taxes to annul the effect of the price reduction. This will not lead to an increase in smuggling if tax enforcement and tax administration is strengthened.

From a technical perspective, are plain packages easier to counterfeit than regular packs?

All visible features and all packs are easy to counterfeit. The quality of counterfeit cigarette packs has substantially improved from the 1990s, making it, in some cases, very difficult to distinguish counterfeit from genuine cigarette packs.

In their 2015 report on plain packaging, HM Revenue and Customs in the UK summarized their findings on counterfeiting as follows: “Currently the quality of counterfeit packaging varies from poorly produced packets to those that are virtually indistinguishable from their genuine counterparts. However, while the introduction of standardized packaging would seem to simplify the counterfeiters’ task, current proposals suggest that future packets would remain complex, with a range of security measures that would present challenges to organized criminal groups, at least in the short term.”

The introduction of plain packaging will not make a difference for counterfeiters: it will remain business as usual.

Luk Joossens, an international expert on tobacco control employed by the Belgian Foundation against Cancer and the Association of European Cancer Leagues, has a Bachelor’s degree (Licence) in sociology from the University of Leuven (1972) and a Master’s degree (Maîtrise) in sociology from the Sorbonne in Paris (1972). He has authored and co-authored many published peer-reviewed papers, including Joossens, L., and M. Raw (2012), “From cigarette smuggling to illicit tobacco trade,” *Tobacco Control* 21: 230-4; Joossens, L., and M. Raw (2008), “Progress in combating cigarette smuggling: Controlling the supply chain,” *Tobacco Control* 17: 399-404; and Joossens, L., and M. Raw (1998), “Cigarette Smuggling in Europe, Who Really Benefits?,” *Tobacco Control* 7: 66-71. Mr. Joossens also wrote a 2012 Cancer Research UK report entitled “Smuggling, the tobacco industry and plain packs.”

More information

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Cigarette plain packaging milestones	
November 2011	Australia passes plain packaging law.
August 2012	The High Court of Australia finds by a 6-1 majority that the plain packaging law is constitutional and not an “acquisition of property,” following a lawsuit filed by JT International and British American Tobacco Australasia Limited.
December 2012	Australia’s plain packaging law takes effect.
April 2014	The report of the independent review undertaken by Sir Cyril Chantler, “Standardized Packaging of Tobacco,” is published in the UK.
March 2015	Ireland passes plain packaging law.
March 2015	The UK passes a plain packaging law covering England.
March 2015	<i>Tobacco Control</i> , which belongs to the <i>British Medical Journal Publishing Group</i> , publishes 14 peer-reviewed papers on plain packaging.
April 2015	The French National Assembly approves plain packaging.
May 2016	Plain packaging laws scheduled to take effect in England, France and Ireland.

Tobacco Control, International Trade, and Public Health: a review of Holly Jarman's book 'The Politics of Trade and Tobacco Control'

By Robert Ireland, Head, WCO Research Unit

Introduction

International trade is subject to conflicts that can arise from, among other things, the inherent tension between business profits and governmental protection of health, safety and the environment. Topics such as plain (standardized) packaging of cigarettes; asbestos (the European Communities – Measures affecting asbestos and asbestos-containing products case); and carbon tariffs (border tax adjustments) in the context of global warming have faced such debate and conflict.

The World Trade Organization's (WTO) core principle for resolving these clashes is in the General Agreement on Tariffs and Trade's (GATT) Article 20 (General Exceptions), which provides that WTO Members can "protect human, animal, or plant life or health" if "such measures are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail, or a disguised restriction on international trade."

The trade in tobacco is a classic public policy example of this dynamic. With respect to public health, cigarettes are unique in that they are the only product that currently can be sold and bought legally but harms the user if consumed as intended. According to the World Health Organization (WHO), six million people died in 2014 from smoking-related diseases; one billion people, mostly in developing countries, are projected to die from smoking-related diseases over the course of the 21st Century.

In addition to their inherent carcinogenic toxicity, cigarettes have the added health detriment - albeit a business advantage to the tobacco industry - of being a highly addictive product which makes cessation a tall obstacle to overcome. On the business side, the tobacco industry grosses enormous amounts of money and employs many workers. An ongoing societal choice is thus whether to prioritize the interests of those who profit from tobacco sales or global public health.

National tobacco control regulations seek to protect human health by restricting all cigarette brands, not just a few chosen ones. In addition to higher tobacco taxes (collected by Customs and other revenue agencies), advertising restrictions and smoking bans in public places, limiting the advertising on cigarette packs with plain packaging is currently at the frontline of tobacco-related public health policymaking. Four countries – Australia, France, Ireland and the United Kingdom – have thus far adopted plain packaging.

Tobacco companies are litigating against plain packaging and are doing so not based on the WTO Article 20 principles but by contending that cigarette pack advertising and logos are trademarks and property rights, and should be protected under the rubric of intellectual property rights and ownership in general.

The Politics of Trade and Tobacco Control

The 2015 book 'The Politics of Trade and Tobacco Control' by Dr. Holly Jarman, a political scientist at the University of Michigan in the United States, examines the intersection of public health, tobacco control and international trade. In addition, the book

describes how lawsuits are being used to challenge public health laws, both in national courts and also in international trade tribunals.

Legal actions against plain packaging laws

Plain packaging and similar tobacco control laws have been subjected to legal actions in three different types of legal forums: (1) national courts; (2) ad hoc tribunals established using provisions from trade or investment agreements; and (3) WTO dispute proceedings.

National courts

After the Australian plain packaging legislation was adopted, but before it entered into effect, tobacco companies filed a lawsuit in 2011 at the High Court of Australia. The plaintiffs contended, among other things, that the plain packaging law should be overturned because it entailed “acquisition of property” – in essence a purported violation of property rights. The Australian High Court upheld the plain packaging law in 2012 in a 6-1 ruling.

Following the adoption of plain packaging laws in England and Ireland in 2015, tobacco companies filed lawsuits in British and Irish courts. These cases are ongoing; the British and Irish governments have indicated that they will defend the cases vigorously.

Uruguay has also instituted a number of robust tobacco control measures, including large graphic health warnings on cigarette packs, bans on misleading words like ‘low-tar’ and ‘light,’ and the limit of one line for the brand name. These measures are part of Uruguay’s efforts to implement the WHO’s Framework Convention on Tobacco Control (FCTC), which it ratified in 2004.

Beginning in 2008, Abal Hermanos – the Uruguayan affiliate of tobacco giant Phillip Morris International (PMI) – and several other tobacco companies, filed lawsuits against Uruguay’s tobacco regulations. In 2009, Abal Hermanos filed a lawsuit at the Supreme Court of Uruguay, alleging, among other things, that its brands had been expropriated. Uruguay prevailed in the national cases.

BIT Tribunals

The so-called Bilateral Investment Treaty (BIT) and Investor-State Dispute Settlement (ISDS) mechanisms are gaining attention in policy circles. Jarman writes that BITs “allow foreign investors to initiate investment disputes against governments that they believe have violated their rights.” The cases are then heard at a legal forum created for the individual investment dispute. The tribunal arbitrators are typically lawyers, one picked by the plaintiff, one picked by the defendant, and one picked by the arbitrators appointed by the parties.

BITs and ISDSs are unusual in that they give private companies the ability to sue governments using bilateral or multilateral governmental treaties, and to do so in a newly established legal forum with several options for a venue. According to leaked text, the draft Trans-Pacific Partnership Agreement (TPP), a regional trade agreement currently being negotiated, includes ISDS provisions.

Uruguay faces a BIT-based case. PMI used a 1988 BIT (ratified in 1991) between Uruguay and Switzerland to request an arbitration tribunal hearing at the International

Centre for Settlement of Investment Disputes (ICSID). The BIT was ratified 13 years before Uruguay ratified the FCTC and 19 years before the PMI BIT-based action. PMI and its affiliates alleged, among other things, that the Uruguayan “80 per cent health warning coverage requirement unfairly limits Abal’s right to use its legally protected trademarks . . .” and caused “a deprivation of PMP’s [Phillip Morris Products] and Abal’s “intellectual property rights.”

The PMI v. Uruguay BIT case is not moving quickly. PMI appointed its arbitrator and Uruguay appointed its arbitrator. They were unable to agree, however, on the third arbitrator, who had to be appointed by the ICSID Secretary General. In 2013, the ICSID agreed that it had jurisdiction to hear the case. The case is expensive for a country of 3.4 million people with a gross domestic product (GDP) of only 57 billion US dollars; Uruguay has apparently received financial support from various sources to defend the case, including from American billionaire and former New York City Mayor Michael Bloomberg.

Similarly, using a 1993 Australia-Hong Kong BIT, a PMI subsidiary launched an action against Australia’s plain packaging law in 2011. PMI alleged that the plain packaging legislation contravened the Australia-Hong Kong BIT “in that they expropriate the investments, are unfair and inequitable, unreasonably impair the use of the investments, amount to a failure to afford full protection and security for the investments, and contravene obligations Australia has entered into with regard to investments of investors, specifically international trade obligations.” PMI also contended that plain packaging is a “technical regulation that is not necessary to fulfill the objective of protection of public health.” Three arbitrators have been appointed – one by PMI, one by Australia and one by the Permanent Court of Arbitration. The case is ongoing.

WTO dispute proceedings

Several countries have launched dispute proceedings against Australia for its plain packaging law at the WTO. The case is expensive both for the complainants and Australia. Jarman cites research indicating that the tobacco industry provided legal and financial support to the countries that lodged the dispute proceedings against Australia.

Ukraine, the first complainant in the WTO proceeding, alleged that the Australian plain packaging law is inconsistent with, among other things, various provisions of the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS Agreement). Several other countries later joined the WTO dispute and a panel was convened.

The action did not make contentions regarding human health and possible discrimination, but placed its hope in contending that stylish advertising on a cigarette pack is intellectual property and should be protected. In May 2015, Ukraine requested that the convened WTO panel suspend its proceedings “with a view to finding a mutually agreed solution.” In June 2015, the panel granted Ukraine's request and suspended its work.

Forum shopping and bulk buying

Jarman writes that the aforementioned tobacco industry strategy is called ‘forum shopping’ and ‘bulk buying.’ She describes forum shopping – or ‘venue shopping’ – as “the practice of selecting the venue, such as an agency, committee, court, or arbitration

body, most likely to provide you with a favourable result.” She describes ‘bulk buying’ as “using multiple forums at once to mediate conflicts over tobacco policy.”

The multiple legal actions against Australia and Uruguay have injected significant complexities and expenses into the adoption of public health regulations. Most likely, the actions have deterred or delayed other countries, especially under-resourced ones, from adopting similar public health laws.

Conclusion

In Australia, data shows that smoking rates have declined and illicit trade has not increased in the period since December 2012 when plain packaging entered into effect. The evidence reflects that plain packaging is working as intended – it is reducing tobacco consumption with no ill effects.

The Australian Border Force (formerly the Australian Customs and Border Protection Service), a WCO Member, has been reporting diminishment in the number of illicit tobacco seizures, one proxy for estimating the illicit trade in tobacco, while taxes have been increasing and plain packaging nears its three year anniversary.

There have been few, if any, examples of counterfeiting of Australian plain packs. One might conclude that the Australian plain packaging law is a technical regulation that is necessary to fulfill the objective of protecting public health and that there is credible evidence that it is reducing smoking prevalence.

More information

www.palgrave.com/

Legal milestones concerning tobacco public health laws*

Date	Legal event
2009	Abal Hermanos (a PMI affiliate) files suit at the Uruguayan Supreme Court against Uruguay's tobacco control laws.
February 2010	Tobacco companies FTR Holding S.A., Philip Morris Products, and Abal Hermanos file a legal action against Uruguay's tobacco control law using a BIT between Uruguay and Switzerland.
November 2010	The Supreme Court of Uruguay unanimously rejects Abal Hermanos's case.
November 2011	A PMI subsidiary files a legal action against Australia's plain packaging law using a BIT between Australia and Hong Kong.
December 2011	Several tobacco companies file a lawsuit against Australia's plain packaging law at the Australian High Court.
March 2012	Ukraine initiates a dispute against Australia for its plain packaging law at the WTO.
April 2012	Honduras initiates a dispute against Australia for its plain packaging law at the WTO.
July 2012	The Dominican Republic initiates a dispute against Australia for its plain packaging law at the WTO.
August 2012	The Australian High Court rules in favour of the Australian plain packaging law.
May 2012	Cuba initiates a dispute against Australia for its plain packaging law at the WTO.
September 2013	Indonesia initiates a dispute against Australia for its plain packaging law at the WTO.
May 2015	Ukraine withdraws its WTO dispute against Australia.

*adapted from Jarman (2015) and the websites of the Australian Government and the WTO.

Higher tobacco taxes increase revenue and save lives: a review of the WHO Report on the Global Tobacco Epidemic, 2015

By Robert Ireland, Head, WCO Research Unit

Taxing tobacco products has historically been a simple way for governments, through their Customs and tax agencies, to collect revenue. Indeed, Adam Smith wrote in his 1776 book *The Wealth of Nations*, “sugar, rum, and tobacco are commodities which are nowhere necessities of life, which have become objects of almost universal consumption, and which are therefore extremely popular subjects of taxation.”

Tobacco taxes are relatively easy to administer, especially if specific excise taxes are used. Moreover, the volume of money currently collected by taxing tobacco is substantial. In 2013 the World Health Organization (WHO) estimated that Customs and other revenue agencies worldwide collected approximately 300 billion US dollars (USD) annually in tobacco tax revenue.

Public health is a second major benefit ensuing from tobacco taxation. This benefit has its basis in the well-established economic principle that higher prices reduce the demand for a product, service, or activity. Economist Paul Samuelson explained that this “downward-sloping demand curve” occurs “when the price of a good is raised (at the same time that all other things are held constant), less of it is demanded.” The *WHO Report on the Global Tobacco Epidemic, 2015*, which this article reviews, examines the policy of higher tobacco taxes.

Reducing negative externalities and internalities

Public policy can raise the price of bad things and also lower the price of good things. Concerning the former objective, reducing negative externalities (bad things impacting third parties) and negative internalities (bad things impacting the self), governments have at their disposal a number of approaches to raise prices. In particular, taxation is an effective and efficient way to raise the price of bad things and thus reduce their usage.

This is, for instance, the leading recommended strategy for mitigating global warming. By raising the carbon price, either with a carbon tax or by emissions trading, carbon pollution will decrease. Concerning this objective, i.e. lowering the price of desired goods, and also in the context of global warming, taxes can be lowered on cars which don't emit carbon dioxide in order to encourage wider purchases and use of electric vehicles.

Another prime policy example of decreasing negative externalities and internalities is tobacco taxation, which raises the price of tobacco products. Higher prices reduce tobacco usage, which subsequently lead to a fall in tobacco-induced diseases and premature deaths. This is not to say that taxes are the only influencer on price; for instance, retail sales prices set by tobacco companies can also be an important factor.

In addition to the policy rationale, there is an international legal basis for the notion that tobacco taxes should be higher for public health purposes. Article 6 of the WHO Framework Convention on Tobacco Control (FCTC) states that “the Parties recognize that price and tax measures are an effective and important means of reducing tobacco consumption by various segments of the population, in particular young persons” and that they should “adopt or maintain measures which may include implementing tax

policies and, where appropriate, price policies, on tobacco products so as to contribute to the health objectives aimed at reducing tobacco consumption.”

Following the adoption of higher tobacco taxes, Customs administrations and other revenue agencies are thus contributing to the dual objectives of increased revenue collection and improved public health.

Types of tobacco taxation: specific excise taxes are best for revenue collection and public health

There are several types of tobacco taxes, such as excise taxes (specific or *ad valorem*), Customs import duties, and value-added taxes (VAT), including goods and services taxes, sales taxes, or purchase taxes. Specific excise taxes are assessed based on the quantity or weight of the product, while *ad valorem* excise taxes are assessed based on the value of the product.

Simplicity is a fundamental characteristic for a tax structure to achieve public policy objectives, and this is why tobacco control experts advocate specific excise taxes on tobacco products. The WHO report, mirroring the WHO FCTC Article 6 Guidelines, supports specific excise taxes as the best way to achieve public health and revenue objectives, particularly because they are easier to administer, and control price movements, when compared with *ad valorem* excise taxes.

Along the same lines, tobacco control expert Dr. Jha Prabhat and several co-authors wrote: “Specific excise taxes are more important insofar as they differentiate tobacco product prices from other prices more than broader taxes do. A high reliance on *ad valorem* and similar taxes by most LIMCs [low- and middle-income countries] creates large price gaps and increases incentives to switch to cheaper products.”

One requirement related to specific excise taxes is that they need to be raised periodically to keep up with inflation. For more extensive analysis of the use of excise taxes in tobacco control, the WHO’s 2010 *Technical Manual on Tobacco Tax Administration* is an excellent primer.

Higher tobacco taxes increase revenue

Although it may seem obvious, higher tobacco taxes increase the amount of revenue collected. Two of the examples cited in the WHO report illustrate this. In Turkey, the tobacco tax rate rose from 58% to 65% of the retail price – cigarette prices tripled, and revenue from cigarette taxes more than doubled between 2005 and 2011. In South Africa, from 1993 to 2009, total cigarette taxes rose from 32% to 52% of the retail price, and the government enjoyed a nine-fold augmentation in revenue yield from tobacco taxation.

Big tobacco tax increases also augment revenue collection even as the number of smokers begins to decline. Research by the World Bank shows “that even very substantial cigarette tax increases will still reduce consumption and increase tax revenues. This is in part because the proportionate reduction in demand does not match the proportionate size of the tax increase, since addicted consumers respond relatively slowly to price rises. Furthermore, some of the money saved by quitters will be spent on other goods which are also taxed. Historically, raising tobacco taxes, no matter how large the increase, has never once led to a decrease in cigarette tax revenues.”

Higher tobacco taxes reduce tobacco usage

Higher tobacco prices lead to decreases in tobacco consumption. The WHO report cites an extensive amount of research that shows how higher tobacco taxes correspond to lower tobacco usage. Three of the examples cited in the WHO report are the United States (US), Brazil, and Turkey:

- Cigarette prices increased nearly 350% in the US between 1990 and 2004, largely due to tax increases. During this time period the percentage of adult American smokers dropped by 33% and the number of cigarettes smoked decreased by more than 50%;
- Brazil experienced similar success. Between 1989 and 2010, the country saw an approximately 46% decline in smoking rates, and most of this was due to higher tobacco taxes;
- As previously mentioned, Turkey increased tobacco taxes while still enjoying higher revenue collection. In addition, between 2008 and 2012, tobacco sales in the country declined by 12% and the prevalence of smoking declined from 31.2% to 27.1%.

Another example is Australia, which in 2010 adopted plain packaging legislation and hiked tobacco taxes by 25%. By 2013, consumption of tobacco products had declined by 11% according to a report released by the Australian Ministry of Finance. Mr. David Crow, the Managing Director of British American Tobacco Australia, said at a government hearing in August 2011 that there “was a 25 per cent increase in the excise and we saw the volumes go down by about 10.2 per cent; there was about a 10.2 per cent reduction in the industry last year in Australia.”

Tobacco price increases and the subsequent decline in usage are relatively similar in rich and poor countries. There is, however, more upside potential in low- and middle-income countries as they tend to have lower tobacco taxes and higher smoking rates. The WHO report summarizes the research on the impact differentials of tobacco price increases for high-income versus low- and middle-income countries in the following Table:

Country type	Tobacco price increase	Range of reduction in tobacco usage	Average reduction in tobacco usage
High-income countries	10%	2.5%-5%	4%
Low- and middle-income countries	10%	2%-8%	5%

Tobacco usage and non-usage can be further understood by considering the terms ‘initiation,’ ‘cessation,’ and ‘intensity.’ Higher tobacco taxes can positively impact each of these dynamics. Many people start smoking when they are teenagers; higher tobacco prices deter some young people from ever starting as they are generally more price sensitive, particularly because they have less disposable income. Cessation (quitting) and lowering intensity (a person who reduces the number of cigarettes they smoke but does not quit) can also be positively impacted by higher tobacco taxes, but face the obstacle of overcoming the addictive power of cigarettes.

Higher tobacco taxes do not lead to rampant illicit trade

Peer-reviewed evidence shows that higher tobacco taxes do not automatically lead to increased illicit trade in tobacco. The illicit trade in tobacco does, however, correlate to weak, inefficient, or corrupt governance which is why building effective, efficient, and less corrupt Customs administrations is important for collecting revenue as well as supporting public health.

One example among many is the United Kingdom (UK). While the nominal price per pack more than doubled from 3.74 British pounds (GBP) in 2000 to 7.13 GBP in 2013, the UK illicit cigarette market share dropped sharply from 21% in 2001 to 9% in 2013. During this period, cigarette usage in the UK declined significantly. This success (higher tobacco taxes, more government revenue, less smoking, and lower illicit trade) was supported by the formulation and implementation of a robust anti-illicit trade in tobacco strategy by UK Customs.

In addition to its public health and revenue successes related to tobacco control, Australia is also experiencing lower illicit trade in tobacco. Although seizures are not a perfect proxy for illicit trade, the volume of tonnes of tobacco seized has been declining while the country continues to put similar resources into countering the illicit trade in tobacco.

A 2015 peer-reviewed research paper by tobacco control expert Dr. Michelle Scollo and three co-authors states that there is “no evidence in Australia of increased use of two categories of manufactured cigarettes likely to be contraband, no increase in purchase from informal sellers, and no increased use of unbranded illicit ‘chop-chop’ tobacco.” Demand for illicit tobacco products is likely to continue to decrease in Australia.

Tobacco taxation rates

An important question for policymakers is what level to set tobacco taxes. The consensus of tobacco control experts is that tobacco taxes should be raised substantially and quickly to achieve government revenue and public health objectives.

The WHO recommends “that excise taxes should account for at least 70% of the retail price of tobacco products, with continued increases above inflation and income growth after reaching this threshold.” The WHO report states that, as of 2014, 33 countries had managed to raise tobacco taxes to 75% of the retail price.

Conclusion

As countries increasingly adhere to the WHO FCTC with higher tobacco taxes, governments will collect more money and facilitate lower tobacco usage. Accordingly, by collecting tobacco taxes, Customs and other revenue agencies are making a vital contribution to human as well as to fiscal health.

More information

www.who.int/tobacco/global_report/2015/en

Quantifying the illicit trade in tobacco: a matter of public interest and self-interest

By Robert Ireland, Head, WCO Research Unit

Scientists determined long ago that there is a direct causal link between smoking and ill-health for both smokers and passive smokers. Despite overwhelming evidence, some stakeholders continued to peddle doubt regarding the health implications until this false contention was no longer tenable.

Research has also shown that tobacco control regulations, such as higher taxes, bans on smoking in public places, advertising bans, purchaser age restrictions, and plain packaging reduce tobacco consumption rates, and thus positively impact human health. Although the evidence for this is conclusive, some stakeholders continue to sow doubt, especially related to the impact of newer regulations, such as plain packaging, on reducing smoking levels.

Opponents of tobacco control also emphasize the non-public health implications, particularly the supposed impact on illicit trade. There is an incentive for certain stakeholders to exaggerate the volume of illicit trade in tobacco, in order to garner resources or to lobby against public policies that result in decreased profits. Also, misleading or false pronouncements are aided by data limitations: illicit trade is difficult to measure because smugglers are not 'eager' to supply data.

Peer-reviewed research, however, generally concludes that although, all things being equal, tobacco control policies such as higher taxes can in some circumstances partially contribute to modest short-term increases in illicit trade, it is not a major factor, and that illicit trade can be better curtailed by policies that strengthen law enforcement and reduce government corruption.

Many examples show that a robust Customs game plan which targets the illicit trade in tobacco, coupled with anti-corruption strategies where necessary, can result in lower illicit trade commensurate with the impact of the implementation of higher tobacco taxes and other tobacco control regulations.

Moreover, even if there are increases in illicit trade, the societal impacts would seem to be inconsequential when compared to the significant benefits of improved public health and greater tax revenue collections. As economist and tax expert Alex Cobham wrote, "there is no doubt that illicit trade in tobacco exists; and nobody argues it's a good thing. But it's clearly not the big issue about tobacco consumption – that would be, er, tobacco consumption."

Illicit trade nomenclature

In their 2011 peer-reviewed paper '*From cigarette smuggling to illicit tobacco trade*,' tobacco control experts Luk Joossens and Martin Raw defined *tax avoidance* as the "purchasing in lower tax jurisdictions of tobacco products by individual tobacco users residing in high tax jurisdictions for their own consumption, within Customs constraints." Thus, tax avoidance is not *per se* an illegal activity.

Tax evasion, however, is an illegal activity. As defined by Joossens and Raw, it "includes the purchase of smuggled and illicitly manufactured tobacco products." The sale of '*cheap whites*' (also known as '*illicit whites*') is a type of tax evasion – the European

Commission has described illicit whites as “brands manufactured legitimately in one market, either taxed for local consumption or untaxed for export, and sold knowingly to traders who transport them to another country where the products are sold illegally without domestic duty paid.”

Smuggling entails cross-border movement of goods that violate Customs laws. *Counterfeiting*, as defined by Joossens and Raw, is the “production of manufactured products which bear a trademark without the consent of the owner of the trademark.”

The broadest term is *illicit trade*, which the World Health Organization’s Framework Convention on Tobacco Control defines in Article 1 as “any practice or conduct prohibited by law and which relates to production, shipment, receipt, possession, distribution, sale or purchase, including any practice or conduct intended to facilitate such activity.”

Tobacco control and illicit trade

Blaming taxation and other government regulations for illicit trade in tobacco has a long history. For instance, 140 years ago in 1876, as reported in Rob Cunningham’s 1996 book *Smoke and Mirrors – The Canadian Tobacco War*, the Tobacco Association of Canada published a guide entitled *Serious Loss of Revenue to the Country*, which “complained that higher taxes had led to a large illicit tobacco trade.”

A more recent example is a tweet by British American Tobacco (BAT) on 24 November 2015, which stated “Excise increases equal *#illegaltobacco* growth.” The tweet linked to a BAT media release criticizing the Australian Government’s increase in tobacco excise taxes. In reality, peer-reviewed research and Australian government data indicate that the illicit trade in tobacco has not increased in tandem with higher tobacco taxes and ‘plain packaging’ in Australia, while smoking rates have declined and revenue collection has increased.

Unwarranted fears of illicit trade have occasionally influenced governments to reduce tobacco taxes, which in turn increases tobacco consumption and tobacco-related diseases, while reducing revenue collection. Actions by the governments of Canada and Sweden in 1994 and 1998 respectively are prime examples of this.

In both countries, tobacco tax increases led to lower smoking rates and higher revenue collection. However, fears about increased illicit trade and political pressure led the governments to reduce the tobacco tax rates, resulting in an increase in smoking rates and a decline in revenue collection.

Interestingly, evidence is presented in Rob Cunningham’s book that in Canada in the 1990s, the rise in illicit trade occurred as a result of Canadian tobacco companies massively increasing exports of Canadian cigarette brands to the United States for which there was virtually no demand, and which were then smuggled back into Canada where demand was high.

It seems almost intuitive that implemented public policies that reduce tobacco consumption would also contribute to lower illicit trade in tobacco, especially over the long-term. If lower initiation, higher cessation, and lower intensity consumption levels ensue for tobacco products compliant with tax regulations, those who quit or never start

will also have less demand for tobacco products that are non-compliant with tax regulations.

Quantifying the illicit trade in tobacco

There are a number of reputable papers that discuss the challenges and methods of quantifying the illicit trade in tobacco. These include the Joossens and Raw paper; the International Agency For Research on Cancer (IARC) handbooks '*Methods for Evaluating Tobacco Control Policies (2008)*' and '*Effectiveness of Price and Tax Policies for Control of Tobacco (2011)*'; and economist and tobacco control expert Dr. Hana Ross's 2015 guide, '*Understanding and Measuring Cigarette Tax Avoidance and Evasion – A Methodological Guide.*'

Of particular importance for consideration are (1) the research methods for measuring the illicit trade in tobacco, and (2) the criteria for evaluating the reliability of papers that present findings on the quantification of the illicit trade in tobacco. Dr. Ross discusses at length criteria for evaluating the quality of papers on illicit trade.

Papers submitted for peer-review which survive the process maintain their credibility, while those that are not formally scrutinized by independent experts do not. In addition, the funding source (if any) should be disclosed – in striving for objectivity and accuracy, it is essential that funding does not come from vested interests expecting a pre-ordained conclusion.

In her guide, while noting the difficulties in obtaining reliable data, Dr. Ross summarizes many of the methods that have been used for measuring the illicit trade in tobacco. She recommends that in striving for the most reliable analysis, it is advantageous for researchers to triangulate (combine different research methods and cross verify from other sources) and to focus on papers that comply with the basic tenets of objective research.

The chart in this article summarizes the 11 tobacco illicit trade research methods discussed by Dr. Ross and a sampling of her comments. Elaboration on the research methods she describes can be accessed at http://tobaccoecon.org/wp-content/uploads/2014/10/Understanding-and-measuring-cigarette-tax-avoidance-and-evasion_a-methodological-guide.pdf.

Chart	
Research Method	Sampling of Dr. Ross's Comments
Survey of tobacco users	<p>"Direct method of estimating the scope of tax avoidance/evasion and availability of low-tax products."</p> <p>"Underestimates tax evasion; problems of validity; potential bias due to social stigma and underreporting"</p>
Exam of cigarette packs obtained from smokers	"Direct and objective method of estimating the scope of tax avoidance/evasion."

	<p>“Tax evasion cannot be detected without self-reported info from smokers and/or lab inspection; possible selection bias.”</p>
Exam of discarded cigarette packs	<p>“Direct and objective method of estimating the scope of tax evasion; can be less expensive than surveys.”</p> <p>“Cannot distinguish tax avoidance from tax evasion; estimates relevant only for narrow geographical areas; difficult to account for tourists/commuters.”</p>
Exam of cigarette packs obtained from retail	<p>“Direct and objective method of estimating the availability of illicit products via legal channels.”</p> <p>“Cannot estimate the scope of tax evasion; cannot detect tax avoidance; lab inspection needed to detect counterfeits.”</p>
Compare sales with consumption (gap analysis)	<p>“Transparent, replicable, and relatively low cost method that uses secondary data; estimates can be generated relatively quickly.”</p> <p>“Lack of reliable survey data; consumer underreporting, tourist purchases and RYO [roll-your-own] cigarettes can bias the results; better at estimating the change rather than the scope.”</p>
Econometric modelling	<p>“Can detect various types of tax avoidance/evasion; can model impact of policies.”</p> <p>“Sensitive to data quality; technically demanding.”</p>
Comparison of tax paid sales with estimated consumption	<p>“Simple and intuitive method.”</p> <p>“Cannot distinguish tax avoidance from tax evasion; better at estimating the change rather than the scope.”</p>
Comparison of actual and projected tobacco tax revenue	<p>“Simple and intuitive method; can detect changes in tax avoidance/evasion.”</p> <p>“Cannot estimate the scope of tax avoidance/evasion; cannot distinguish tax avoidance from tax evasion; cannot detect one time deviation from a trend.”</p>
Key informant interviews	<p>“Little technical skills required; low costs; relatively quick assessment of the situation.”</p> <p>“Subjectivity of the estimates; may generate</p>

	bias results.”
Monitoring tobacco trade	<p>“Can detect smuggling hubs.”</p> <p>“Cannot estimate the scope of tax avoidance/evasion for individual countries; captures only large-scale tax evasion.”</p>
Analysing seizures of illegally transported tobacco	<p>“Globally, the World Customs Organization (WCO) provides annual data on tobacco seizures from its Customs Enforcement Network.”</p> <p>“Can generate the minimum scope of tax evasion. Can inform on the composition of the illicit market.”</p> <p>”Information may not be complete or easily available, and it could be difficult to establish its accuracy.”</p> <p>[The focus on] “large seizures may not be representative of the illicit market as a whole.”</p> <p>“Underestimate the scope of tax evasion; sensitive to enforcement effort.”</p>

Source: Ross (2015)

No silver bullet for quantifying the illicit tobacco trade

A perfect method or methodology by which to measure the illicit trade in tobacco does not exist. Any study that contends that one particular methodology can make a definitive conclusion concerning the measurement of illicit trade should be disregarded. By using several methods that comply with objective research rules, reasonable estimates can in some settings be made. Moreover, illicit trade cannot be viewed in isolation; smoking rates and revenue collections from tobacco taxes are not only easier to measure, but are vital matters for public policy.

The Trans-Pacific Partnership Tobacco Carve-Out Precedent

By Robert Ireland, Head of WCO Research Unit¹

The Trans-Pacific Partnership (TPP) text includes an article allowing the parties the ability to deny the possibility of challenges to their tobacco control measures under the Investor-State Dispute Settlement (ISDS) provisions. Several TPP parties as well as public health advocates had sought this “tobacco carve-out” to prevent transnational tobacco companies (TTCs) from using the TPP to challenge tobacco control laws, particularly cigarette plain packaging requirements, as they have done using bilateral investment treaties (BITs). TTCs had lobbied the negotiators not to include the tobacco carve-out in the TPP. Regardless if the TPP is ultimately ratified by the parties, the TPP tobacco carve-out will likely be precedent for the insertion of language protecting tobacco control measures in future bilateral and multilateral international trade and investment treaties. Moreover, the TPP tobacco carve-out is another in a growing list of legal and policy defeats for TTCs. This article summarizes the state-TTC conflict that influenced and resulted in the TPP tobacco carve-out.

1 Introduction

Scientists long ago established a clear correlation between smoking and diseases such as lung cancer, heart disease, and emphysema, and thus premature death. The World Health Organization (WHO) estimates that 6 million persons are killed every year by tobacco-related disease. In addition, the financial costs for treating tobacco-induced illnesses are substantial. Acting on this knowledge, many governments in recent decades have passed tobacco control laws with the objective of curtailing smoking and thus reducing tobacco-related disease and the ensuing exorbitant health care costs. Such public health laws have included measures such as bans on tobacco advertising, bans on smoking in public places, minimum sales ages for purchasers, higher tobacco taxes, warning labels on cigarette packs, and most recently plain (standardized) packaging. National tobacco control measures are also part of efforts to implement the WHO’s Framework Convention on Tobacco Control (FCTC).² Such policy methods for protecting human health have, and will always have, some degree of incompatibility with the business interests of tobacco producers which gross enormous amounts of money, employ many workers, and seek to sell as many cigarettes as possible. To protect these interests, transnational tobacco companies (TTCs) have sought to overturn national public health regulations, especially by litigation.

Increasingly, the conflict between advocates of tobacco control and TTCs is playing out in international trade forums, such as Investor-State Dispute Settlement (ISDS) tribunals

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² WHO Framework Convention on Tobacco Control, Feb. 27, 2005, 2302 U.N.T.S. 166 [hereinafter “FCTC”].

and the World Trade Organization (WTO). The two most prominent targets of TTC litigation are tobacco control pioneers Australia and Uruguay, particularly their policies on restricting the content and appearance of cigarette packs. In countries where tobacco advertising is largely prohibited, cigarette packs are the last prominent advertising medium. Australia was the first country to adopt a plain packaging policy and Uruguay has also regulated the content and appearance of cigarette packs. Consequently, these two countries have been the main targets of TTC litigation challenging cigarette pack advertising regulations. In addition, several WTO members, with legal³ and financial⁴ support from the tobacco industry, have initiated dispute proceedings at the WTO against Australia challenging its plain packaging law. The TTC claims have focused not on the human health issues⁵ but rather on commercial issues, particularly alleged trademark infringement and property rights violations.

The legal wrangling between the combatants has now impacted the Trans-Pacific Partnership (TPP), where the agreed text includes a provision that would curtail the ability of TTCs to challenge tobacco control laws using the TPP investor-state dispute proceeding (ISDS) provisions. This article opines on the TPP tobacco carve-out and summarizes the cases that influenced it.

2 The TPP Tobacco Carve-Out

The draft TPP full text was published in November 2015 and includes a provision that limits the ability of tobacco companies to use ISDS provisions to challenge tobacco control measures. The draft TPP text states:

³ *Financial Times* (2012), “Big Tobacco backs Australian law opposers,” reporter Christopher Thomson, April 29, 2012.

⁴ *The Times* (2012), “Big Tobacco fights back on packaging,” reporter Jonathan Ames, December 12, 2012; *Reuters* (2015), “Ukraine drops WTO action against Australian tobacco-packaging laws,” reporter Tom Miles, June 3, 2015.

⁵ The WTO’s General Agreement on Tariffs and Trade’s (GATT) Article 20 (General Exceptions) provides that WTO Members can “protect human, animal, or plant life or health” if “such measures are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail, or a disguised restriction on international trade.”

Article 29.5: Tobacco Control Measures

A Party may elect to deny the benefits of Section B of Chapter 9 (Investment) with respect to claims challenging a tobacco control measure¹³ of the Party. Such a claim shall not be submitted to arbitration under Section B of Chapter 9 (Investment) if a Party has made such an election. If a Party has not elected to deny benefits with respect to such claims by the time of the submission of such a claim to arbitration under Section B of Chapter 9 (Investment), a Party may elect to deny benefits during the proceedings. For greater certainty, if a Party elects to deny benefits with respect to such claims, any such claim shall be dismissed.

¹² For greater certainty, this Article does not prejudice: (i) the operation of Article 9.14 (Denial of Benefits); or (ii) a Party's rights under Chapter 28 (Dispute Settlement) in relation to a tobacco control measure.

¹³ A tobacco control measure means a measure of a Party related to the production or consumption of manufactured tobacco products (including products made or derived from tobacco), their distribution, labeling, packaging, advertising, marketing, promotion, sale, purchase, or use, as well as enforcement measures, such as inspection, recordkeeping, and reporting requirements. For greater certainty, a measure with respect to tobacco leaf that is not in the possession of a manufacturer of tobacco products or that is not part of a manufactured tobacco product is not a tobacco control measure.

In essence, Article 29.5 would thus prevent tobacco companies from using the TPP agreement to challenge tobacco control laws in ISDS tribunals. In addition, Article 29.5 of the TPP could set a precedent for future bilateral and multilateral trade and investment agreements to restrict the ability of the tobacco industry to challenge public health laws focused on tobacco.

3 Legal Actions against Australia's Plain Packaging Law

3.1 Australia's Plain Packaging Law⁶

The Australian *Tobacco Plain Packaging Act 2011* (TPPA) was adopted on November 21, 2011, and entered into force on December 1, 2012. The concept of plain packaging has been part of tobacco control policy discourse since the 1980s⁷ and is recommended in the FCTC and the FCTC Guidelines.⁸ As described by two scholars, the TPPA's main components are "to make it an offence to sell tobacco products not in plain packaging; to require packaging to be a standardized, featureless (except for prominent graphic health warnings), drab dark-brown with the font for the brand name also standardized, and

⁶ *Tobacco Plain Packaging Act 2011* (Cth) s 19 (Austl.); *Tobacco Plain Packaging Regulations 2011* (Cth) reg 2.2.1 (Austl.).

⁷ Liberman, Jonathan (2013), "Plainly Constitutional: The Upholding of Plain Tobacco Packaging by the High Court of Australia," *American Journal of Law and Medicine* 39, 361.

⁸ *Ibid*, 361-362.

cigarette sticks standardized without trademarks.”⁹ Concurrent to plain packaging implementation, cigarette consumption has continued to decline in Australia.¹⁰

3.2 TTCs challenge the TPPA at the Australian High Court

Four TTC companies - British American Tobacco (BAT), Imperial Tobacco, Japan Tobacco International (JT), and Philip Morris International (PMI) - have challenged the TPPA in Australia’s High Court.¹¹ After the Australian plain packaging legislation was adopted, but before it entered into effect, BAT filed a lawsuit in 2011 at the High Court of Australia. BAT alleged, among other things, that the plain packaging law would “result in an acquisition of their property rights otherwise than on just terms.”¹² The Australian Government responded “that the Plaintiffs’ claimed rights have always been the subject of restrictions arising from Commonwealth, State or Territory legislation and the common law. It further submits that the provisions of the TPP Act do not amount to an acquisition of the Plaintiffs’ property within the meaning of section 51(xxxi) of the Constitution.”¹³ Several days later, JT filed a similar lawsuit claiming “that its rights in both the Trade Marks and the Get Up are “property” for the purposes of section 51(xxxi) of the Constitution” and that TPPA provisions “constitute an acquisition of its property otherwise than on just terms.”¹⁴ The defendant responded as it did in the related case.

The Australian High Court upheld the plain packaging law in 2012 in a 6-1 ruling and concluded that “neither the Commonwealth nor any other person acquired any property and s 51(xxxi) was not engaged.”¹⁵ The Court explained that “[t]here can be no acquisition of property without ‘the Commonwealth or another acquir[ing] an interest in property, however slight or insubstantial that it may be.’”¹⁶ “[T]he relevant constitutional question is whether there has been an acquisition of property, not whether there has been a taking.”¹⁷ The TTCs were ordered to pay the Commonwealth’s costs.¹⁸

⁹ Clarke, Harry and David Prentice (2015), “Interview of Harry Clarke and David Prentice by Robert Ireland,” *WCO News*, No. 76, 62.

¹⁰ Joossens, Luk (2015), “Interview of Luk Joossens by Robert Ireland,” *WCO News*, No. 77, 69-70.

¹¹ Liberman, 367.

¹² *British American Tobacco Australasia & Ors v. The Commonwealth of Australia* (S389/2011), Short Particulars.

¹³ *Ibid.*

¹⁴ *JT International SA v. The Commonwealth of Australia* (S409/2011), Short Particulars.

¹⁵ *JT International SA v. Commonwealth of Australia* 250 CLR; 86 ALJR 1297, 291 ALR 5 Oct 2012, Case Number: SA092011 S389/2011, High Court Judgement.

¹⁶ *JT Int’l SA v. The Commonwealth of Australia*, as quoted in Liberman, 370.

¹⁷ *Ibid.*

¹⁸ Liberman, 371.

3.3. TTCs challenge the TPPA at an ISDS tribunal

Using a 1993 Australia-Hong Kong Bilateral Investment Treaty (BIT), a PMI subsidiary filed a request for arbitration concerning Australia's plain packaging law in 2011. PMI alleged that the plain packaging legislation was in conflict with the Australia-Hong Kong BIT "in that they expropriate the investments, are unfair and inequitable, unreasonably impair the use of the investments, amount to a failure to afford full protection and security for the investments, and contravene obligations Australia has entered into with regard to investments of investors, specifically international trade obligations."¹⁹ PMI also contended that plain packaging is a "technical regulation that is not necessary to fulfill the objective of protection of public health."²⁰ In addition to pecuniary relief, PMI sought injunctive relief, which is unusual in ISDS tribunals.²¹ As is the norm in ISDS tribunals, three arbitrators were appointed – one by PMI, one by Australia and one by the Permanent Court of Arbitration. The seat of arbitration was Singapore. On December 17, 2015, the tribunal unanimously dismissed the case on jurisdictional grounds.

3.4 TTCs challenge the TPPA at the World Trade Organization

With financial and legal support from TTCs, several countries have launched dispute proceedings against Australia for its plain packaging law at the WTO.²² Ukraine, the first complainant in the WTO proceeding, alleged that the Australian plain packaging law is inconsistent with, among other things, various provisions of the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS Agreement). Honduras, the Dominican Republic, Cuba, and Indonesia later joined the WTO dispute and a panel was convened. In May 2015, however, Ukraine requested that the convened WTO panel suspend its proceedings "with a view to finding a mutually agreed solution." In June 2015, the panel granted Ukraine's request and suspended its work. The other WTO countries have not as of yet requested suspension.

4 Legal actions against Uruguay's tobacco control measures

4.1 Uruguay's tobacco control measures

In 2008-2009, Uruguay instituted a number of tobacco control measures through ministry ordinances and presidential decree, including large graphic health warnings on cigarette packs, bans on misleading words like 'low-tar' and 'light,' and the limit of one line for the

¹⁹ PM Asia v. Commonwealth of Australia, Notice of Arbitration, 2011.

²⁰ Ibid.

²¹ Ritwik, Ankita (2013), "Tobacco Packaging Arbitration and the State's Ability to Legislate," *Harvard Law Review*, Volume 54, Number 2, Summer 2013, 523.

²² WTO DISPUTE DS434, "Australia — Certain Measures Concerning Trademarks and Other Plain Packaging Requirements Applicable to Tobacco Products and Packaging."

brand name.²³ In addition, each company was allowed only one product: “[e]ach brand of tobacco shall possess a single form of presentation.”²⁴

4.2 TTCs challenge Uruguay’s tobacco control measures

Beginning in 2008, Abal Hermanos – the Uruguayan affiliate of PMI – and several other tobacco companies, filed lawsuits against Uruguay’s tobacco control regulations. In 2009, Abal Hermanos filed a lawsuit at the Supreme Court of Uruguay, alleging, among other things, that its brands had been expropriated. Uruguay prevailed in the national cases.²⁵

4.3 TTCs challenge Uruguay’s tobacco control measures at a ISDS tribunal

Uruguay now faces a BIT-based arbitration case. PMI used a 1988 BIT (ratified in 1991) between Uruguay and Switzerland to request arbitration at the International Centre for Settlement of Investment Disputes (ICSID). The BIT was ratified 13 years before Uruguay ratified the FCTC and 19 years before the PMI BIT-based action. PMI and its affiliates alleged, among other things, that the Uruguayan “80 per cent health warning coverage requirement unfairly limits Abal’s right to use its legally protected trademarks . . .” and caused “a deprivation of PMP’s [Phillip Morris Products] and Abal’s “intellectual property rights.”²⁶ The PMI v. Uruguay BIT case is advancing slowly. PMI has appointed its arbitrator and Uruguay has done the same. They were unable to agree, however, on the third arbitrator, who had to be appointed by the ICSID Secretary General. In 2013, the ICSID agreed that it had jurisdiction to hear the case.²⁷

Conclusion

The accumulating TTC legal defeats and the TPP tobacco carve-out are major developments in the conflict between government health policies and tobacco company business interests. While three other countries (Ireland, the United Kingdom, and France) have adopted plain packaging²⁸ it is likely that more countries will now feel confident to do so as a result of the governments prevailing in all of the cases decided thus far. In each instance, the *de facto* result of the court and tribunal decisions has been that human health should be prioritized over the commercial interests of one industry. While this would seem self-evident from a normative perspective, it has become increasingly apparent from a legal perspective. It is likely that in future bilateral and multilateral trade and investment agreement negotiations, an increasing number of

²³ Jarman, 77-85; Ritwik, 524.

²⁴ Uruguayan Ministry of Health, Ordinance 466.

²⁵ Jarman, 77-85.

²⁶ *Ibid.*

²⁷ *Ibid.*

²⁸ Ireland and the United Kingdom have already been sued by TTCs in domestic courts for alleged intellectual property rights violations.

countries will demand tobacco carve-outs to protect their tobacco control public health laws.

Table 1 Legal milestones on the way to the TPP Tobacco Carve-out

Date	Legal event
February 27, 2005	WHO Framework Convention on Tobacco Control (FCTC) is adopted.
2009	Abal Hermanos, S.A. v. Uruguay commences at the Supreme Court of Uruguay.
February 2010	Philip Morris v. Uruguay, ICSID Case No. ARB/10/7 commences based on the Uruguay-Switzerland BIT.
November 2010	The Supreme Court of Uruguay unanimously rules in favor of Uruguay in Abal Hermanos, S.A. v. Uruguay .
November 21, 2011	Australia's Tobacco Plain Packaging Act 2011 is adopted.
November 2011	Philip Morris Asia Limited v. The Commonwealth of Australia, UNCITRAL, PCA Case No. 2012-12 commences based on the Australia-Hong Kong BIT.
December 1, 2011	British American Tobacco Australasia Limited and Ors v. The Commonwealth of Australia commences at the Australian High Court
December 12, 2011	JT International SA v. Commonwealth of Australia commences at the Australian High Court.
March 2012	Ukraine initiates a dispute against Australia for its plain packaging law at the WTO. Honduras, the Dominican Republic, Cuba, and Indonesia join the dispute later.
August 2012	The Australian High Court rules 6-1 in favor of the Australian plain packaging law.
December 1, 2012	Australia's Tobacco Plain Packaging Act 2011 enters into force.
May 2015	Ukraine withdraws its WTO dispute against Australia.
November 2015	TPP Full Text published including the tobacco carve-out (Article 29.5).
December 17, 2015	PMI's BIT case against Australia is dismissed.

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