

CONTROLLING ILLCIT TOBACCO TRADE:



A GLOBAL REVIEW OF COUNTRY EXPERIENCES

GEORGIA: CONTROLLING ILLICIT CIGARETTE TRADE

TECHNICAL REPORT OF THE WORLD BANK GROUP
GLOBAL TOBACCO CONTROL PROGRAM.

EDITOR:
SHEILA DUTTA



GEOORGIA

5

GEORGIA:

Controlling Illicit Cigarette Trade

Hana Ross and George Bakhturidze¹

Chapter Summary

Georgia represents a success story in the fight against illicit tobacco trade, because it has managed to substantially increase tobacco taxes while reducing the presence of illicit tobacco products in its domestic market. Although the official numbers on illicit trade are incomplete, particularly regarding the border with Russian-controlled areas of Georgia, there are several reliable indicators pointing to limited domestic trade in illicit tobacco products, thanks to vigorous action to strengthen the effectiveness of customs and tax administration.

The major risk of large-scale illicit trade in Georgia is related to export/import business, as Georgia seems to play the role of a transit country for illicit tobacco products, most of them destined for Turkey. Small-scale smuggling is not an issue, since cigarette prices in Georgia are roughly similar to those of its neighbors – except for Turkey, where taxes and prices are far higher. Thus, cross-border shopping does not play a significant role in reducing tobacco tax revenues in Georgia, whether through smuggling (tax evasion) or legal imports (tax avoidance). Tax avoidance, however, is a major problem in Georgia, because tobacco taxes for cigarettes without filters are substantially lower than those for filtered cigarettes,

¹ H. Ross (University of Cape Town, South Africa) and G. Bakhturidze (FCTC Implementation & Monitoring Center, Georgia)

and the tobacco industry exploits this administrative loophole. Another tax avoidance tactic practiced by the industry is forestalling: ordering a larger-than-needed quantity of tax stamps just before a tax increase in order to use these less-expensive stamps after the tax increase comes into effect.

The tobacco industry has, at times successfully, argued against tobacco tax increases on the grounds of illicit trade, pointing to the decline in tobacco tax revenue following a tax increase. However, a closer look at the data shows that the illicit trade story does not hold. In fact, the lower revenue was artificially created by the industry's practice of forestalling. Since it took the market some time to absorb the packs with the old/lower tax stamps, tax revenue receipts immediately after the tax increase were lower, allowing the industry to spread a misleading interpretation of the tax measure's impact on illicit tobacco trade.

Georgia has recently taken a major step toward compliance with the World Health Organization Framework Convention on Tobacco Control (WHO FCTC), which it has signed, by banning tobacco advertising and substantially expanding smoke-free places. Nevertheless, cigarettes in Georgia are still relatively inexpensive, and smoking prevalence, particularly among men, is extremely high.

Georgia's experience supports prior research findings that strengthening the effectiveness of customs and tax administration is by far the most important step to counteract illicit tobacco trade. The concluding section of this chapter offers specific recommendations in line with this result. These recommendations include:

Tackle forestalling. Georgia should adopt measures to prevent firms from buying tax stamps in anticipation of announced tax increases (forestalling). Adopting anti-forestalling measures would lead to gains in tax revenue.

Ratify the Protocol. Georgia should also ratify the Protocol on Illicit Trade, since the additional obligations under the Protocol would be minimal, given that Georgia already uses modern technology to control its cigarette supply chain. Being a party to the Protocol would reinforce the progress made to date in improving the effectiveness of customs and tax administration and allow Georgia to play a role in addressing the transit of illegal cigarettes via its territory.

Rapidly align with the Protocol and the European Union (EU) system. The government should analyze the extent to which its current system is compliant with the FCTC Illicit Trade Protocol and the EU track-and-trace system to be introduced in 2019. The Protocol, for example, requires licensing of economic operators involved in the tobacco product supply chain. Georgia should, therefore, reinstitute its licensing requirement, at least for cigarette manufacturers, importers, and exporters.

Reinforce border protections and product movement control systems. Georgia should enhance the protection of its vulnerable border with Abkhazia and Ossetia by video monitoring of all trucks entering and leaving the country from those territories. Such a surveillance

system could be supported by road cameras and mobile X-rays, and integrated with the e-Transport and the excise marking electronic system.

Reinforce international cooperation. Georgia should consider strengthening cooperation and information exchange with EU Member States, especially with those bordering Russia (e.g., Poland, Estonia, Lithuania), since they are facing similar illicit trade problems, and with its neighbor countries. As in the case of collaboration with the UK Customs office, Georgia can enhance its interaction with Interpol, the European Anti-Fraud Office (OLAF), and other relevant agencies in the fight against illicit tobacco trade.

Bring government-tobacco industry relations in line with international norms.

Government should amend its legislation to comply with Article 5.3 of the FCTC regarding tobacco-industry interference in policy making. The most relevant provisions for controlling the illicit tobacco market are requirements that the tobacco industry and/or its affiliates cannot be involved in discussions related to the ITP ratification or a track-and-trace system.

1. Background

Tobacco production and consumption in Georgia: historical trajectory. As the part of the Soviet Union, the Republic of Georgia was well known for tobacco growing, supplying leaves both for Georgia's own domestic cigarette production and for production in other Soviet territories (Shalutashvili et al. 2007; WB 1996).

The production of raw tobacco and cigarettes collapsed following the fall of the Soviet Union. In 1993–1994, Georgia's tobacco crop was only one-third that of what it had been in 1987 (Ciecierski and Chaloupka 2002). This decline continued until the mid-2000s. During 1991–2005, the size of tobacco fields shrank from 14 thousand hectares to 0.8 thousand hectares, the production of raw tobacco dropped from 23 thousand tons to 1.5 thousand tons, and cigarette output fell from 17 billion to 3 billion cigarettes (State Department of Statistics 2006).

Penetration of transnational firms. This was a great opportunity for transnational tobacco companies to enter Georgia to exploit its extremely high smoking prevalence. In 2001, 53.3 percent of males and 6.3 percent of females smoked. By 2008, the prevalence had risen to 59.8 percent and 14.9 percent among men and women, respectively (Bakhturidze. et al. 2008; Gilmore. et al. 2004). In 2002, 32.6 percent of boys and 12.1 percent of girls aged 13 – 15 reported being current cigarette smokers (GYTS Georgia, 2002).² International evidence shows that roughly half of regular smokers die prematurely as a result of tobacco-related diseases, losing on average two decades of expected life. For the whole population of regular smokers, life expectancy drops by about a decade.³ Thus, Georgia's smoking pandemic is a cause of grave concern for the health and life expectancy of Georgians.

² 2002 Global Youth Tobacco Survey (GYTS), Georgia Report. 2002.

³ Peto and Jha. Global Effects of Smoking, of Quitting, and of Taxing Tobacco. *New England Journal of Medicine*. 2014; 370:60-68; <https://www.nejm.org/doi/full/10.1056/nejmra1308383>

By the early 1990s, three major tobacco companies (Philip Morris, British American Tobacco, Japan Tobacco International) were present in the market, taking advantage of a loose regulatory environment that allowed them to run promotional campaigns encouraging smoking. Only two locally-owned manufacturers out of seven present in 1993 survived the foreign invasion: Tbilisi Tobacco (previously Georgian Tobacco – GTM), and Omega Group Tobacco (OGT) (Shalutashvili et al. 2007).

The Georgian government welcomed the tobacco industry by allowing them to sell tobacco tax-free. Between 1991 and 1997 there was no tax on either locally produced or imported cigarettes. The situation changed in 1997, when imported cigarettes were levied a specific excise and customs tax of 0.25 GEL (about US\$ 0.19) and 0.19 GEL (about US\$ 0.15) per pack of filter and non-filter cigarettes, respectively. Locally produced cigarettes, on the other hand, were levied an excise tax worth 100 percent of their production costs. The following year, both imported and domestic cigarettes were levied a specific excise tax with substantially lower rates for domestic cigarettes. This differential tax treatment of domestic and imported cigarettes persisted till 2010 (Table 1).

Post 2004: new directions in tobacco policy. Between 1998 and 2004 the tax rates remained stable, but their values were eroded by inflation, which hovered around 5 percent most years, with a peak of 19 percent in 1999 (State Department of Statistics 2004). Taking account of annual growth in per capita income of about 6 percent in that period, cigarettes became increasingly affordable, by about 10 percent per year. The new government of Mikheil Saakashvili came into power in 2004 and announced substantial tobacco tax hikes effective January 2005. This measure was motivated essentially by revenue concerns, rather than public health. The tax more than doubled on imported filtered cigarettes and more than tripled for domestic filtered cigarettes (Table 1). As a result, the tax share in the retail price jumped from 36 percent to 54 percent for imported cigarettes, and from 25 percent to 43 percent for domestic cigarettes. However, the tax rate on non-filtered cigarettes remained about one-fourth of that on filtered cigarettes.

Tobacco company “forestalling.” Tobacco companies had six months to prepare for the 2005 tax increase. They pre-purchased tax stamps⁴ at the lower 2004 value for release in 2005, thus realizing tax savings in 2005 (Krasovsky 2013; Shalutashvili et al 2007). This resulted in an unexpected increase in tobacco tax revenue in the second part of 2004 and disappointing revenue in 2005. The tobacco excise tax revenue in 2005 was 72 million GEL, about 4.4 million GEL less compared to 2004, when the revenue was artificially increased by firms’ pre-purchasing the tax stamps (Figure 1). The industry, however, blamed illicit cigarette trade for the revenue shortfall, claiming that the market share of illicit cigarettes went from 10 percent in 2003 to 65 percent after the tax hike (Shalutashvili et al 2007).

⁴ Georgia adopted excise stamps on both domestic and imported cigarettes on February 1, 1999 (Shalutashvili et al. 2007).

A closer analysis reveals that the combined 2004/2005 tobacco excise tax revenue was 65 percent (148 million GEL) higher than the 2002/2003 revenue (90 million GEL) in nominal terms, and 47 percent higher in real terms. This demonstrates that the tax increase did bring significant additional revenue for the government. However, the tobacco industry was able to manipulate the story about the lower 2005 tax revenue, which the industry itself had caused, persuading the government to reduce the tobacco excise tax in 2006, “to decrease smuggling.” This was a sharp blow to Georgia’s tobacco tax policy, and it took the country almost ten years to return to the 2005 rates (Table 1).

Table 1. Evolution of Georgia’s Excise Rates Per Pack of 20 Cigarettes (GEL)

| | 1991 - 1997 | 1997 | 1998 | 2001 | 2005 | MAY 2006 | 2010 | SEPT 2013 | 2014 | 2015 | 2016 | 2017 | 2018 |
|-------------------------------|-------------|-------------------------|------|------|------|----------|------|-----------|------|---------------|------|------|------|
| Imported with filter (GEL) | No tax | 0.25 | 0.25 | 0.4 | 0.9 | 0.6 | 0.6 | 0.75 | 0.75 | 0.9 | 1.1 | 1.7 | 1.7 |
| Imported without filter (GEL) | No tax | 0.19 | 0.19 | 0.2 | 0.25 | 0.15 | 0.15 | 0.2 | 0.2 | 0.25 | 0.3 | 0.6 | 0.6 |
| Local with filter (GEL) | No tax | 100% of production cost | 0.15 | 0.2 | 0.7 | 0.4 | 0.6 | 0.75 | 0.75 | 0.9 | 1.1 | 1.7 | 1.7 |
| Local without filter (GEL) | No tax | 100% of production cost | 0.05 | 0.07 | 0.15 | 0.1 | 0.15 | 0.2 | 0.2 | 0.25 | 0.3 | 0.6 | 0.6 |
| Ad valorem rate. % | | | | | | | | | | 5 (from July) | 10 | 10 | 10 |

Source: Georgian Tax Code 2000, 2004, 2005, 2006, 2009, 2017; Shalutashvili et al. 2007.

2. Recent Evolution of Georgia’s Tobacco Control Policies

Tobacco control measures under the FCTC. In 2006, Georgia ratified the WHO Framework Convention on Tobacco Control (FCTC) and committed itself to carry out a set of measures to decrease the alarmingly high smoking prevalence in the country.

Since one of the most cost-effective measures to curb tobacco use is increasing tobacco taxes,⁵ the government and local NGOs pay particular attention to tobacco tax policy. Following a challenge by British American Tobacco at the World Trade Organization (WTO), the government equalized the excise tax rates for imported and locally manufactured cigarettes in 2010 by raising the rate for domestic cigarettes to the level for imported cigarettes (Table 1). This policy change is in line with the best practice in tobacco taxation. On the

⁵ Tobacco Tax Reform At The Crossroads Of Health And Development. Edited by Patricio Marquez and Blanca Moreno-Dodson. World Bank. October 2017

other hand, the persistent gap between the tax rates on filtered and non-filtered cigarettes goes against WHO recommendations on tobacco tax policy⁶ and encourages downward substitution instead of reduction in smoking.

In addition to its tobacco tax policy, Georgia has implemented other tobacco control measures following the ratification of the FCTC. The 2008 Tobacco Control Law banned smoking in educational, medical, sport, and cultural facilities, while other indoor facilities had to have designated smoking areas. As a result, bars and restaurants allowed smoking in up to 50 percent of their premises. The law also prohibited the sale of cigarettes to/by minors and the sale of cigarettes in places where toys or children's clothing were sold. The legislation banned cigarette sales within 50 meters of schools. Tobacco advertisement was banned on TV/radio and within 100 meters of schools and bridges. Since 2009, it is prohibited to accept sponsorship from the tobacco industry (Law on Advertisement of Georgia 2009).

In 2010, the law introduced new packaging regulations requiring health warnings to cover 30 percent of the pack. However, the enforcement of these tobacco control laws was weak, also due to frequent court challenges against the legislation. In addition, no proof of age was required to purchase tobacco products (Bakhturidze et al. 2016). As a result, a 2014 survey showed that 77 percent of Georgian adolescents had no difficulty in buying tobacco products at points of sale.⁷

Association with the European Union: implications for tobacco control. In 2014, Georgia signed an association agreement with the European Union (EU-Georgia Association Agreement 2014). According to the Agreement, Georgia is obliged to harmonize its tax policy, including tobacco tax policy, with that of the EU. As a result, Georgia adopted a mixed tobacco tax system in 2015 by adding an ad valorem component to the excise duty. The base for calculating the ad valorem tax is retail prices set each year by order of the Ministry of Finance (MoF 2017). In addition, substantial tax increases took place in 2015, 2016, and 2017 with the goal of reaching the current EU tax level (1.8 Euro per pack, or about 5.2 GEL) within about seven or eight years following the Association Agreement. These tax increases resulted in a higher share of tax in the retail price and in additional tax revenue. (Figure 1)

As of January 1, 2018, filter cigarettes incur a specific excise tax of GEL 1.70 (0.70 USD) per 20 cigarettes, and non-filter cigarettes a specific tax of GEL 0.60 (0.25 USD) per 20 cigarettes, independent of their origin. In addition, each pack is also levied 10 percent ad valorem excise (Tax Code 2018). Excise taxes are also levied on pipe/loose tobacco at GEL 35 (14.5 USD) per kilogram. This translates to GEL 0.50 (0.20 USD) per pack, assuming 0.7 g of tobacco per cigarette, a rate lower than non-filtered cigarettes.⁸ Only about 2.5 percent of smokers in Georgia use roll-your-own tobacco (ISSA 2016). All tobacco products are also subject to 18 percent VAT.

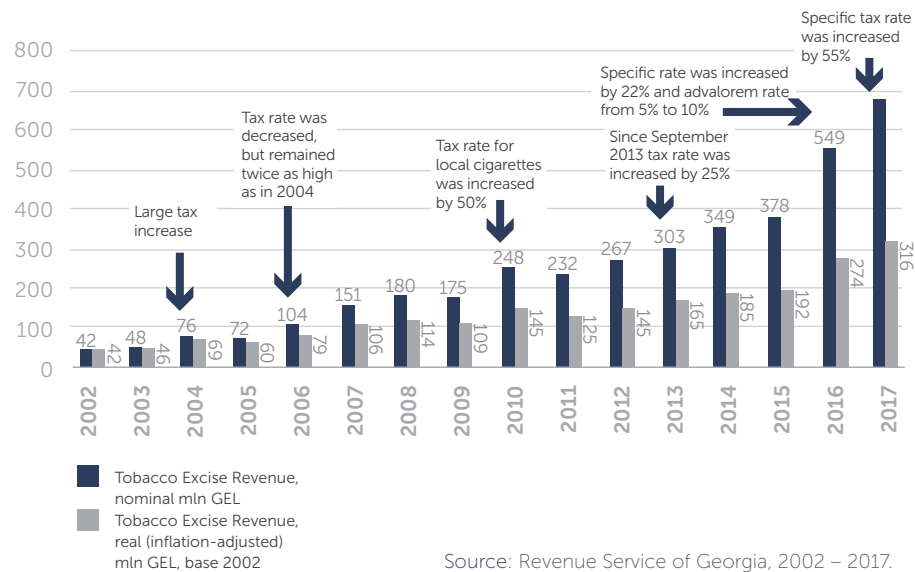
⁶ Guidelines for implementation of Article 6, WHO FCTC, 2014.

⁷ Global Youth Tobacco Survey, Georgia, 2014

⁸ Hana Ross, Report on Technical Assistance Visit to Georgia, 4 - 12 September, 2017.

Starting on August 1, 2017, Georgia began to tax e-cigarettes (0.2 Gel, or 0.08 USD, per 1 mg of liquid) as well as cartridge and iQOS devices (GEL 1.7, or 0.7 USD per piece) (Tax Code 2018).

Figure 1. Tobacco Excise Revenue in Georgia 2002–2017, Nominal and Real (Million GEL)

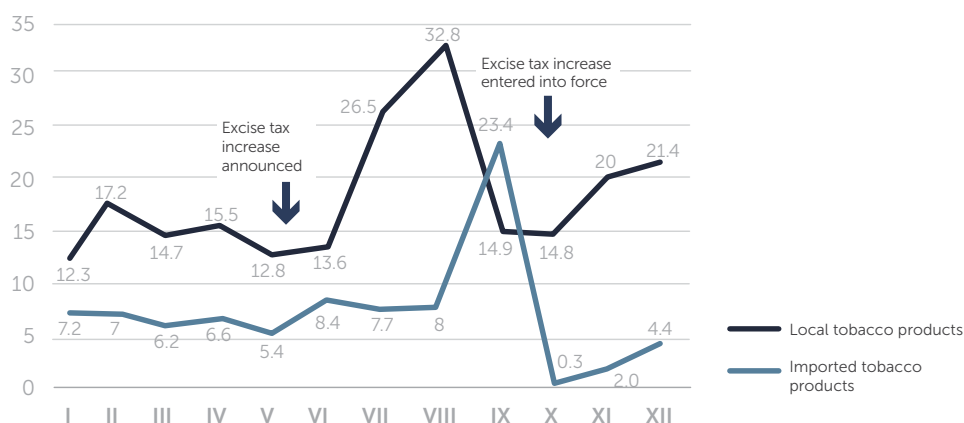


Forestalling continues. The tobacco industry is still engaged in forestalling. Figure 2 demonstrates this behavior in 2013. A tax increase was announced in June 2013, effective September 1, 2013. The excise revenue from local cigarettes reached 23.4 million GEL in September 2013, three times more than the previous month, reflecting tax stamp purchases just before the tax increase. The tax receipts for the rest of the year amounted to only 63 million GEL. Despite industry tax avoidance, total excise tax revenues reached 303 million GEL in 2013, 13 percent more than in 2012.

Similar behavior was recorded in 2017, when the industry requested 14.6 percent fewer excise tax stamps compared to 2016 (Table 2). Despite this pattern, 2017 excise revenue increased by 123 million GEL compared to 2016, thanks to the higher tax rate (Figure 1).

Maneuvers by the industry makes it challenging to study the reaction of the market to recent tax increases. As noted, rather substantial tax increases occurred in September 2013 and then each January in 2015, 2016, and 2017. The tobacco industry responded to the 2013 tax increase by an overproduction/over-importation of cigarettes (Figure 2) before the tax increase. Therefore, a drop in the size of the market was expected in 2014. The demand for tax stamps declined in 2014, but the size of the market actually increased in that year, based on official statistics concerning local production, import, and export (Table 2). The 2015 tax increase kept the demand for tax stamps almost constant, but the size of the market shrank. Comparing the size of the market and the demand for tax stamps in 2013 with 2016, we

Figure 2. Monthly Excise Tax Revenue in 2013, Nominal, Million GEL



Source: Revenue Service of Georgia, 2014.

observe a decline in both statistics, signaling that the decline in the number of cigarette sold after the 2013 tax increase was real. However, the size of the cigarette market in 2017 was almost identical to its size in 2013 (Table 2). This is likely related to the affordability of cigarettes, explored below.

The cigarette re-export phenomenon. In 2017, the gap between the market size and the number of cigarettes based on the excise marks sold increased dramatically. This is likely related to cigarettes for re-export, a phenomenon that began in 2014. These cigarettes, imported to Georgia to be re-exported to a third country, are not featured in the import/export statistics, but are recorded in a separate line (Table 2). The import for re-export is not taxed, but it incurs a service fee for processing, bringing additional revenue to Georgia. Re-exported cigarettes are likely to escape excise taxation in the destination country, thus supplying the black market.⁹ The primary destination for the re-export used to be Turkey, where cigarettes are more expensive compared to Georgia. However, the recent collaborative agreement between Georgia and Turkey, adopted in 2017, successfully blocked this pathway.¹⁰ Therefore, the top destinations for re-export in 2017 were Azerbaijan (1,218.5 million sticks), Kazakhstan (1,146.4 million), and Singapore (249.4 million) (National Statistics Office of Georgia 2018).

Another interesting development was a massive decline in domestic production and an increase in imports during 2010 - 2017. Domestic production represented about 33 percent of the total market in 2013, but its share had dropped to about 18 percent by 2017. Legal exports tend to fluctuate but do not represent a significant portion of the market (Table 2).

⁹ Interview with the former head of Georgia Customs Service and a representative of the Georgia Revenue Service.

¹⁰ Interview with a representative of Georgia Customs Service conducted March 18, 2018.

Table 2. The Cigarette Market in Georgia, 2010–2017, Million Sticks

| MILLION PIECES/ YEARS | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 |
|--|---------|---------|---------|----------|----------|---------|----------|----------|
| A: Domestic production | 5,002.0 | 4,429.0 | 3,813.0 | 3,463.7 | 3,128.1 | 1,888.3 | 1,670.6 | 1,857.4 |
| B: Export | 21.0 | 0 | 1.0 | 10.1 | 151.9 | 352.8 | 68.5 | 149.2 |
| C: Import | 4,492.0 | 5,261.0 | 5,991.0 | 6,953.4 | 8,242.2 | 7,968.5 | 8,441.1 | 9,206.0 |
| Market Size (=A-B+C) | 9,473.0 | 9,690.0 | 9,803.0 | 10,407.0 | 11,218.4 | 9,504.0 | 10,043.2 | 10,914.2 |
| Re-export | 0 | 0 | 0 | 0 | 27.4 | 402.3 | 704.8 | 2,764.2 |
| Number of cigarettes based on the excise marks sold | NA | NA | NA | 9,898.4 | 9,717.9 | 9,745.7 | 9,296.9 | 7,943.3 |

Source: National Statistics Office of Georgia 2018 and the Revenue Service 2018.

Evolution of the domestic cigarette market: unexpected directions. Given the tobacco excise tax increases in recent years and the declining size of the population,¹¹ one would expect the Georgian market to shrink. However, Table 2 shows otherwise. To investigate the issue, Table 3 presents the estimates of affordability of three different types of cigarettes sold in Georgia. We have used a standard method to measure affordability, calculating it as the share of per capita GDP needed to purchase 100 cigarette packs in one year.¹² Results show that the affordability is increasing, with a declining percentage of per capita GDP needed to purchase 100 cigarette packs.

The affordability of all cigarette types increased between 2000 and 2017. It took 6.48 percent of per capita GDP to buy 100 imported cigarette packs in 2000, but only 3.77 percent of per capita GDP to do so in 2017, for example. This is not a positive development from a public health perspective, since the affordability of products, which captures the impact of both prices and income, is an important driver of consumption. The affordability trend explains the limited impact of higher taxes on the size of the market in Georgia. On a positive note, the affordability of cigarettes declined in 2017 compared to the previous year, though this trend is likely not to be sustained since no tax increase took place in 2018.

A quick market observation in September 2017 revealed that the cheapest (non-filtered) cigarettes cost GEL 1.25 per pack (about \$0.50), while the prevailing price of a non-filtered cigarette pack was GEL 1.30 per (about \$0.54). Premium cigarettes were sold for about GEL 4 per pack (\$1.65). The substantial tax increases in recent years, together with the persistence of the price difference between filtered and non-filtered cigarettes due to the two-tiered tax system, motivated some consumers to switch to the cheaper non-filtered

¹¹ United Nations, Department of Economic and Social Affairs, Population Division. World Population Prospects: The 2017 Revision.

¹² Blecher, C and P van Walbeek. International analysis of cigarette affordability. *Tobacco Control* 2004;13:339–346. doi: 10.1136/tc.2003.006726

Table 3. Cigarette Affordability in Georgia, RIP, 2000–2017

| YEAR | AFFORDABILITY LOCAL WITHOUT FILTER | AFFORDABILITY LOCAL WITH FILTER | AFFORDABILITY IMPORTED WITH FILTER |
|------|------------------------------------|---------------------------------|------------------------------------|
| 2000 | 1.84% | 3.30% | 6.48% |
| 2001 | 1.54% | 4.81% | 6.64% |
| 2002 | 1.29% | 4.75% | 5.77% |
| 2003 | 1.06% | 3.86% | 4.77% |
| 2004 | 1.13% | 3.77% | 4.51% |
| 2005 | 1.31% | 5.00% | 5.51% |
| 2006 | 1.15% | 3.34% | 5.31% |
| 2007 | 0.90% | 3.43% | 4.25% |
| 2008 | 0.79% | 2.73% | 3.70% |
| 2009 | 0.84% | 2.74% | 3.86% |
| 2010 | 0.89% | 2.50% | 3.46% |
| 2011 | 0.87% | 2.31% | 3.08% |
| 2012 | 0.82% | 1.97% | 3.39% |
| 2013 | 0.85% | 2.11% | 3.52% |
| 2014 | 0.86% | 2.13% | 3.19% |
| 2015 | 0.92% | 2.25% | 3.20% |
| 2016 | 0.99% | 2.38% | 3.13% |
| 2017 | 1.21% | 2.98% | 3.77% |

Source: Authors' calculation based on data from the Statistical Office of Georgia. RIP = relative income price

cigarettes. According to the Revenue Service of the Ministry of Finance, the sales of excise tax stamps for non-filtered cigarettes doubled in 2017.

A 25-gram bag of loose tobacco sold for GEL 3, a pack-equivalent of GEL 1.7 (\$0.71).¹³ This is slightly more compared to non-filtered cigarettes, despite lower tax rates on loose tobacco. Nevertheless, only 2.5 percent of smokers roll their own cigarettes. Cheap devices for rolling cigarettes costing GEL 3 (about \$1.25) are available on the market (ISSA 2016).¹⁴

Getting around the regulations: enforcement falls short. Despite a ban, sale of single cigarettes is easily observed on the streets of Tbilisi. The prices range from 7.5 to 10 tetri (about

¹³ Hana Ross. Report on Technical Assistance Visit to Georgia. 4 - 12 September. 2017

¹⁴ Hana Ross. Report on Technical Assistance Visit to Georgia. 4 - 12 September. 2017.

3 – 4 US cents), a pack-equivalent of 1.5 – 2 GEL, which means that there is a premium charged for selling single cigarettes.¹⁵ The possibility of acquiring a cigarette so inexpensively reduces the economic barrier to smoking initiation, even though the premium should reduce the number of cigarettes smoked per day. The Code of Administrative Offenses effective since May 1, 2018, allows the revenue authority to issue a penalty on the spot in the amount of GEL150 (\$61) for single cigarette sales (Law on Tobacco Control 2018, Law on Advertisement 2018). Implementation and enforcement of the law are still low priorities.

Even though tobacco advertising has been banned since 2009, tobacco companies have found ways to advertise new brands through banners, sponsorship programs, and displays at checkouts. As recently as September 2017, the Georgian capital was flooded with billboards promoting cigarettes. This changed on May 1, 2018, when Georgia amended its tobacco control legislation to cover all tobacco products including e-cigarettes and hookahs, for example. The new law bans smoking in public places (with only a few exceptions, such as casinos, cigar bars, and private taxis) as well as all forms of advertising and promotions. (Outdoor displays will be banned from September 1, 2018, while indoor displays will be banned from January 1, 2021.) Pictorial health warnings covering 65 percent of the front of the pack will become obligatory from September 1, 2018, and plain packaging will enter into force from December 31, 2022. Proof of age is now required to purchase tobacco products (Law on Tobacco Control 2018).

Stubbornly high prevalence rates and tobacco-related mortality. As result of the high affordability of cigarettes and the fact that major tobacco control policy advances have for the most part occurred recently, the effort to reduce smoking prevalence has had only moderate success. In 2016, 57 percent of men and 7 percent of women reported current smoking, while a cotinine test suggests that close to 12.2 percent of women smoke (STEPS 2016). The majority of smokers (90.5 percent) are daily smokers. About 16.5 percent of boys and 7.8 percent of girls aged 13–15 years consume tobacco products.¹⁶ These statistics put Georgia on the list of countries with the highest smoking prevalence, both in Europe and worldwide.

The death toll from tobacco use in Georgia is correspondently large – about 11,400 deaths or 22 percent of all deaths in the country are attributable to smoking every year. Tobacco use imposes a substantial economic burden on society, amounting to about 825 million GEL (345 million USD) per year, equivalent to 2.4 percent of GDP. Out of this amount, 327 million GEL (135 million USD) are related to healthcare. This represents 13 percent of Georgia’s total public healthcare expenditures (UNDP 2018).

¹⁵ Hana Ross. Report on Technical Assistance Visit to Georgia. 4 - 12 September. 2017.

¹⁶ Global Youth Tobacco Survey. Georgia. 2014.

3. Tax Avoidance and Tax Evasion

The transition period toward democracy after the collapse of the Soviet Union was characterized by several conflicts with Russia that resulted in the separation of regions of Abkhazia and South Ossetia from Georgia. High levels of corruption also marked this period.

Conflict, corruption, and illicit trade. This situation created fertile soil for illicit trade in tobacco products. Smugglers took advantage of the vulnerable borders between Georgia, Abkhazia, and South Ossetia. Domestic manufacturers evaded paying taxes by declaring cigarettes for export while selling them tax-free in Georgia. The authorities regularly detected false excise tax stamps and noticed excise tax stamps being used just on cartons instead of on individual packs. Illegal cigarettes, mostly with Russian excise tax stamps and/or Russian health warnings, were easily found (Shalutashvili et al. 2007).

A 2002 survey revealed that only two-thirds of the cigarettes on the market had the correct excise mark, with only one-third of imported cigarettes falling into that category. The majority of non-compliant imported cigarettes had a Russian tax stamp.¹⁷ In addition, about 62.5 percent of the domestic cigarettes on the market were produced in non-registered facilities.¹⁸

A survey conducted one year later, in 2003, reported that only 32.5 percent of the cigarette brands sold in Georgia were legal. About 31 percent of brands were sold without an excise stamp or with an excise stamp from a foreign country, while the remaining 36 percent of brands were sold both legally (with the proper excise stamp) and illegally (without the excise stamp or with an excise stamp from another country) (Kobeshavidze et al. 2003). One study estimated that, from 1997 to 2003, illicit cigarettes represented 50 percent and 30 percent of the cigarette market in rural and urban areas, respectively (Shalutashvili et al. 2007). Euromonitor reported similar figures (Table 4).

Post-2004 reforms: reining in illicit tobacco. The reforms initiated in 2004 by the new government focused on economic revival while addressing corruption and widespread tax evasion. Large-scale changes at the Ministry of Finance and the Georgia Customs Services (which falls under the Ministry of Finance) improved tax administration so that, by 2005, the number of registered cigarette manufacturers doubled compared to 1995, as formerly unregistered entities were forced to enter the ranks of registered companies (Shalutashvili et al. 2007). Georgia's ranking in the Corruption Perceptions Index by Transparency International improved strikingly, from rank 133 in 2004 to 67 in 2008 and further to 51 in 2012, surpassing several EU countries. The economy began to grow, and the state budget increased by 300 percent between 2004 and 2007.¹⁹ A doubling of tobacco excise tax revenue contributed to this progress, thanks to a higher tobacco tax rate and improved tobacco tax administration (Figure 1). The World Bank named Georgia as the leading economic

¹⁷ Supply and Use of Tobacco Goods in Georgia. State Department for Statistics of Georgia. Tbilisi, 2002.

¹⁸ Supply and Use of Tobacco Goods in Georgia. State Department for Statistics of Georgia. Tbilisi, 2002.

¹⁹ Mikheil Saakashvili. Wikipedia. https://en.wikipedia.org/wiki/Mikheil_Saakashvili Accessed June 6, 2018.

Table 4. Illicit Trade Market Share in Georgia

| YEAR | SHARE OF ILLICIT % (2016) | SHARE OF ILLICIT % (2017) |
|------|---------------------------|---------------------------|
| 2001 | 40.60 | NA |
| 2002 | 40.30 | 51.63 |
| 2003 | 36.70 | 47.84 |
| 2004 | 34.40 | 45.41 |
| 2005 | 36.90 | 48.08 |
| 2006 | 12.20 | 18.06 |
| 2007 | 7.20 | 10.98 |
| 2008 | 4.20 | 6.53 |
| 2009 | 1.50 | 2.41 |
| 2010 | 0.80 | 1.34 |
| 2011 | 0.60 | 0.88 |
| 2012 | 0.60 | 0.88 |
| 2013 | 0.30 | 0.42 |
| 2014 | 0.30 | 0.40 |
| 2015 | 0.30 | 0.42 |
| 2016 | NA | 0.44 |

Source: Euromonitor 2016 and 2017.

Note: The reliability of Euromonitor data has been questioned,²⁰ and the data for Georgia are not consistent between 2016 and 2017 reports. However, the trend reported by Euromonitor has been corroborated by other reports.

reformer in the world and noted that "Georgia's transformation since 2003 has been remarkable. The lights are on, the streets are safe, and public services are corruption-free."²¹

Because of these changes, the illicit trade in cigarettes declined dramatically, despite the increasing tax and even though cigarette prices in Georgia became for some period of time higher compared to neighboring countries (Krasovsky 2013). According to Euromonitor, the largest drop in the illicit cigarette market occurred between 2006 and 2009 (Table 3). By 2017, the Head of the Healthcare Committee of the Georgian Parliament reported that the illicit cigarette market share was less than 3 percent of total consumption (Commersant 2017-1), a truly remarkable reduction from the high levels discussed above and shown in Table 4.

²⁰ Evan Blecher, Alex Liber, Hana Ross, Jo Birckmayer. Euromonitor data on the illicit trade in cigarettes. *Tobacco Control* 2015. 24:100-101

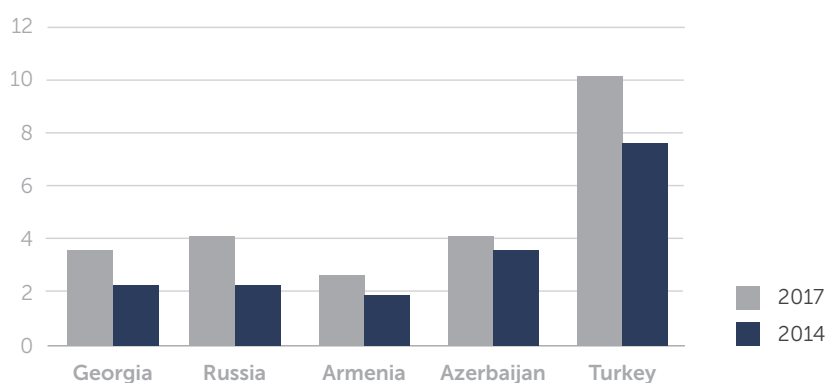
²¹ Mikheil Saakashvili. Wikipedia. https://en.wikipedia.org/wiki/Mikheil_Saakashvili Accessed June 6, 2018.

Table 5. Nominal Prices (GEL) for Selected Cigarette Brands, 2014 and 2017

| BRAND | GEORGIA | | RUSSIA | | ARMENIA | | AZERBAIJAN | | TURKEY | |
|-----------|---------|------|--------|------|---------|------|------------|------|--------|------|
| | 2014 | 2017 | 2014 | 2017 | 2014 | 2017 | 2014 | 2017 | 2014 | 2017 |
| Marlboro | 3 | 4 | 2.8 | 4.5 | 2.3 | 3.2 | 4 | 5 | 9.5 | 11 |
| Winston | 2.2 | 3.5 | 2.2 | 4 | 1.8 | 2.6 | 3 | 4 | 7.5 | 10 |
| Pall Mall | 2 | 3 | 1.8 | 3.5 | 1.6 | 2.2 | 2.8 | 3.5 | 7 | 9 |

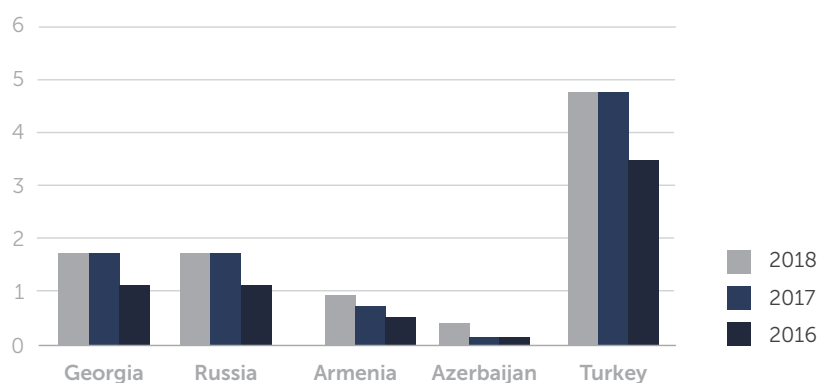
Source: <https://worldcigaretteprices.com>; MPOWER 2015; WHO Global Tobacco Control Report, 2017; tabacum.ru

Figure 3. Prices of Winston Brand Cigarettes in Georgia and Its Neighbors, 2014 and 2017



Note: Winston is the most popular imported brand in Georgia and Turkey.

Figure 4. Cigarette Excise Tax Rates in Georgia and Neighboring Countries, 2016–2018, in GEL



Source: Tax Laws of Georgia, Russia, Turkey, Armenia, and Azerbaijan. Data in GEL provided by Konstantin Krasovsky.

Note: Minimum specific excise tax rates are shown; tax in Georgia does not include the ad valorem component.

This would be in line with the estimates of the MoF (about 2 percent of the total market in 2017²²) and Euromonitor (Table 4).

Cross-border dynamics. The motivation for cross-border shopping varies from country to country, but the recent excise tax increases in Georgia made this activity less profitable (Table 5, Figure 3, and Figure 4). Georgia has four land neighbors: Turkey, Russia, Armenia, and Azerbaijan. Cigarette prices in Turkey are about three times higher than in Georgia, due to substantially higher excise taxes. As a result, Turkey does not pose a threat to the Georgian domestic cigarette market, but cigarettes seem to be smuggled from Georgia to Turkey. There are some reports that the proceeds from this business are funding the Kurdistan Workers' Party (PKK), recognized as a terrorist organization by Turkey, the EU, and the United States (Daily Sabah 2015; Eurasianet 2014; Hurriyet Daily News 2015; Panorama 2015). To address the issue, Georgia, in collaboration with Turkey, adopted strengthened control measures in 2017, preventing organized crime groups from smuggling cigarettes from Georgia to Turkey and other countries surrounding the Black Sea.²³

Russian excise tax rates are similar to those in Georgia, but cigarette prices are higher in Russia.²⁴ However, the Georgian territories Abkhazia and South Ossetia, controlled by Russia, could potentially be a source of illicit tobacco products (discussed below).

Cigarettes in Armenia are the most tempting for cross-border shopping (which could be either legal or illegal, depending on the quantity), because cigarette prices in Armenia are about 20 – 25 percent lower than in Georgia. The price difference stems from the difference in excise taxes – the Armenian excise is around 50 percent lower than that applied in Georgia.

Authorities' current concerns. Officials of the Georgia Revenue Service, which includes the Customs Service, have stated that the main issues that currently worry them are (a) small-scale cigarette smuggling related to other criminal activities and (b) transit of illicit cigarettes through Georgia.²⁵ Small-scale cigarette smuggling usually involves small trucks or cars and takes the form of bootlegging or "ant smuggling" (frequent cross-border movement of small amounts of cigarettes). This is considered a comparatively minor problem. The movement of illegal cigarettes from Russia, Armenia, Azerbaijan, or Ukraine via Georgian territory to third-country destinations (often Turkey) is of greater concern.

The tax-avoidance challenge. Even though tax evasion is a minor issue in Georgia, the country has a problem with tax avoidance. In addition to forestalling, tobacco companies are taking advantage of the tax differential between filtered and non-filtered cigarettes. In 2015, in response to the growing gap between filtered and non-filtered cigarettes, local manufacturers began to manufacture non-filtered cigarettes with an elongated empty end suitable for

²² Hana Ross. Report on Technical Assistance Visit to Georgia. 4 - 12 September. 2017.

²³ An interview with a representative of Georgia Customs Service conducted March 18, 2018.

²⁴ Federal Tax Service of Russia. <http://service.nalog.ru/tabak.do>

²⁵ Customs Service presentation during the Georgia mission of the European Network for Smoking and Tobacco Prevention (ENSP), December 2017.

inserting filters. The filters are offered separately at the point of sale free of charge. This tax avoidance saves a company 1.1 GEL (USD 0.45) on a pack of cigarettes (based on 2018 tax rates) and encourages downward substitution that increases the affordability of cigarettes. This industry behavior would explain the doubling of non-filtered cigarette sales in 2017.

4. Measures to Control Tax Avoidance and Tax Evasion

Tax stamps. All tobacco products sold in Georgia are subject to taxation and must bear an excise tax stamp, except for pipe tobacco. Excise tax stamps were first introduced in 1999 as a tax-collection instrument, meaning that manufacturers and importers pay taxes by purchasing these fiscal stamps. The security features on the stamps were initially minimal, making them vulnerable to counterfeiting. The authorities also reported multiple uses of single tax stamps.²⁶ Since their introduction, tax stamps have evolved substantially, making them much more secure, as described below in the section on the tracking and tracing system.

Excise duties and VAT are payable when the goods are supplied to the final consumer or upon removal from the warehouse facility for sale. Importers pay these taxes at the time of import (Revenue Service of Georgia 2018; Tax Code of Georgia 2018).

The Department of Standards, in charge of the content of tobacco products, was dissolved in 2005. In the same year, raw tobacco was excluded from the Ministry of Agriculture's regulatory jurisdiction (Petriashvili et al. 2016). Raw tobacco intended for manufacturing tobacco products is exempt from excise taxes.

Shifts in the approach to licensing. Georgia introduced licensing of tobacco manufacturing and packaging in 1999 (Law on Licensing of Production of Food and Tobacco Products 2010). Unfortunately, the law was suspended towards the end of 2005 (Law on Licensing and Permissions 2005) and abolished by 2009 (Law on Licensing of Production of Food and Tobacco Products 2010). Therefore, no license is currently required to import, export, or distribute tobacco products in Georgia.

Duty-free shops selling tobacco products must have a license issued by the Revenue Service of Georgia and are obligated to assist Customs in executing their control authority (Revenue Service of Georgia 2012). The retail sale of tobacco products via Internet or mail is prohibited since May 1, 2018 (Law on Tobacco Control 2018).

Customs Service enforcement activities. The Georgia Customs Service has already implemented several measures to control illicit trade in tobacco products. For example, it runs a risk analysis and assessment system to select suspicious trucks for inspection. It uses X-ray

²⁶ Alexander Shalutashvili, Hana Ross, Judith Watt, Stephanie Hilborn, George Bakhturidze, Gela Kobeshavidze, Zaza Grigalashvili. Tobacco Economic Study in Georgia since the Fall of the Soviet Union. Editor: George Magradze. Open Society Institute. Tbilisi, Georgia, November 2007.

scanners at all border crossings and at the postal sorting center²⁷ to detect suspicious cargos and packages. It employs trained dogs that can recognize nicotine. However, only about 2 percent of containers with imported excisable goods are being randomly inspected. If a container has cigarettes, 2 percent of cartons are chosen, and then 2 percent of packs from those cartons are selected for inspection.²⁸

As of January 2018, international travelers can bring either 200 cigarettes (reduced from the previous 400 cigarettes) or 50 cigars or 50 cigarillos or 250 grams of other tobacco products or 10 capsules for e-cigarettes to Georgia tax free (Tax Code of Georgia 2018). For those using a land border, this limit applies for a period of 30 calendar days to prevent “ant” tax avoidance.²⁹

There are penalties for selling illegal cigarettes. The first offense calls for a fine ranging from 1000 to 2000 GEL (USD 400 to 800). The second offense within the same year is subject to a penalty of 10,000 GEL, or USD 4,000.³⁰

Implementing an integrated control system. In November 2011, the Georgia Revenue Service launched a competitive bid for an “Integrated System of Movement and Registration of Products.” Seven companies submitted proposals, and in the end the contract was awarded to SICPA, a company based in Switzerland.³¹ The system, which became operational in March 2013, requires all packs intended for the domestic market to carry a paper-based fiscal stamp with a high level of security features (overt, semi-covert, and covert). These stamps are unique, secure, and non-removable. Each stamp contains information stored in a serialized code intended for tracking and tracing and for a data management system. This information includes the name of producer or importer, product name, time and place of production, and volume. The data management system is located at the Georgia Revenue Service, and the information sent to the data center is transmitted in near real time. A web application allows domestic producers and importers to order, forecast, pay, and activate the fiscal stamps. This electronic system of excise marking imposes an immediate control by identifying the producer, the product, and how the product entered the market.

Even though the system is capable of both tracking and tracing, it is currently used only for tracing. The Georgia Revenue Service is currently satisfied with its performance. Revenue Service field officers carry hand-held inspection devices allowing them to authenticate products in retail distribution.

²⁷ X-rays at post offices are not a high priority due to the low prevalence of tax evasion via those channels.

²⁸ Hana Ross. Report on Technical Assistance Visit to Georgia. 4 - 12 September. 2017.

²⁹ “Ant” tax avoidance is defined as making frequent journeys across the border with the legally allowed amounts of tobacco products for the purpose of making profit.

³⁰ Hana Ross. Report on Technical Assistance Visit to Georgia. 4 - 12 September. 2017.

³¹ Information provided by a SICPA representative on 25 January 2017.

Packs intended for export carry a bar code indicating the destination country.³² An additional benefit of strengthening tobacco tax administration was spillover to tax administration of other products. In 2012, the SICPA system was expanded to cover alcohol and beer, then further extended to non-alcoholic beverages in 2016. The cost of the system (5 Euro/1000 stamps) is just a bit more than the previous simple tax stamp system. These expenses are initially covered by the government, but starting in 2018 the industry must cover the costs.³³

International collaboration. Regarding international collaboration, Georgia is a member of the World Trade Organization, and its Ministry of Finance has a memorandum of understanding with the UK Customs office to share intelligence regarding large-scale smuggling operations.³⁴ Even though Georgia was involved in the negotiations related to the FCTC's Protocol to Eliminate Illicit Trade in Tobacco Products, which was adopted by the Conference of Parties in 2012 (WHO 2012), unfortunately it has yet to ratify the Protocol.

Recent seizures of illicit cigarettes. The Investigative Services unit of the Ministry of Finance seized 61,419 and 557,685 packs of illegal cigarettes in 2016 and 2017, respectively. Simultaneously, the Customs Service of Georgia reported 96,896 and 228,071 cigarette packs that were not declared in those two years, respectively, even though only a portion of them were intended for sale in Georgia (Ministry of Finance of Georgia, 2018³⁵). For example, in October 2017, Customs seized 113,600 packs of Armenian cigarettes destined for Russia (Sputnik – Georgia, 2017). Based on the health warnings, these cigarettes were produced in Armenia for export to Iraq, but "got lost" on their way.³⁶ The growing number of seizures can be linked to the growing re-export business, which makes the country vulnerable to leaks from trade volumes not intended for the domestic market. The seized cigarettes are destroyed, but the Ministry of Environment and National Resources Protection has yet to establish an environmentally friendly method to dispose of these products.

Given the number of cases of seizure and the revenue loss estimated at 950,000 GEL in 2017 (tobacco excise revenue reached 672 million GEL in that year), the Ministry of Finance does not suspect any systematic violation of the tobacco excise tax law, except for the situation near the uncontrolled territories (Abkhazia and South Ossetia) and near the border with Armenia (Ministry of Finance of Georgia, 2018). The Georgian Ministry of Interior Affairs (MIA) reported only five criminal cases related to illicit tobacco trade in 2016, while it investigated seven such cases in 2017 (MIA of Georgia 2018). The MIA Border Police reported no criminal violations during the period 2013–2017 (Border Police of Georgia, 2018).

³² Tobacco Products Taxation Policy, National Diseases Control Center. 2016.

³³ Hana Ross. Report on Technical Assistance Visit to Georgia. 4 - 12 September. 2017.

³⁴ Hana Ross. Report on Technical Assistance Visit to Georgia. 4 - 12 September. 2017.

³⁵ Despite the Rise of Smuggling, Cigarette Sales Did Not Fall. *Commerzant*, April 2018; <https://commerzant.ge/en/post/despite-the-rise-of-smuggling-cigarette-sales-not-fell>

³⁶ A resident of Georgia found almost 30 thousand packs of contraband cigarettes in the attic. *Black Sea Press*, 16 May 2017. <https://www.newsgeorgia.ge/u-zhitelya-gruzii-obnaruzhili-na-cherdake-pochti-30-tysyach-pachek-kontrabandnyh-sigaret/>

Misinformation on seizures and illicit tobacco flows. Despite the remarkable record of Georgia's authorities in controlling illicit trade, the tobacco industry and associated groups persist in drawing attention to illicit cigarette trade. Industry spokespersons commented, for example, on the higher number of seizures in 2017, erroneously claiming that illicit trade in cigarettes increased 18-fold (Commersant 2017-II). In this context, it is important to note that seizures are not the best indicator of the level of illicit trade activity, since they are also a function of the intensity and the level of law enforcement.

The industry's multipronged strategy. The tobacco industry continues to interfere with Georgia's excise tax policy. It organizes seminars for both high- and mid-level MoF officials, particularly focusing on the Central Administration, Revenue Service, and Investigation Units (Academy of MoF, 2013). Even though since 2009 it is prohibited to receive sponsorship from the tobacco industry (Law on Advertisement of Georgia 2009), the transnational tobacco companies provide funding to various public agencies (e.g., Rondeli Foundation, the Police Academy), as well as several universities (e.g., Caucasus School of Business, Tbilisi State University, Sokhumi State University, Free University).

5. Conclusions

Georgia is an example of a country that successfully brought the illicit market in tobacco products under control, thanks to progressive economic reforms targeting, among other institutions, its Revenue and Customs services. In a relatively short period of time, Georgia managed to reduce corruption, set up effective tax administration and enforcement, and institute strong border control as key components of its strategy to control illicit trade in tobacco products. As a result, Georgia has managed to substantially decrease tax avoidance through various administrative measures, while pursuing a policy of regularly increasing cigarette excise taxes.

The data reveal the highest level of tax evasion during 1997 – 2003, when excise tax rates were about four- and eight-times lower on imported and domestic cigarettes, respectively, than in 2017. Yet the illicit cigarette market in 2017 is reported to be negligible. This confirms the empirical evidence from other countries pointing to the relatively small role of cigarette taxes as drivers of illicit cigarette trade. Georgia's experience adds to the growing body of evidence that tobacco tax increases can boost revenue even as vigorous enforcement keeps the illicit tobacco trade under control.³⁷

The remaining issues for the Georgian authorities to address are related to weak administrative borders with Abkhazia and South Ossetia, occupied by Russia, cross-border activities

³⁷ The Economics of Tobacco and Tobacco Control. National Cancer Institute Tobacco Control Monograph 21. NIH Publication No. 16-CA-8029A. Bethesda, MD: U.S. Department of Health and Human Services. National Institutes of Health. National Cancer Institute; and Geneva: World Health Organization; 2016. <https://cancercontrol.cancer.gov/brp/tcrb/monographs/21>

along the Armenian border, and possible movement of illegal goods across Georgian territory to other countries. Ratifying the Illicit Trade Protocol would provide Georgia with more tools to address these loopholes in its system.

Only the substantial excise tax increase in 2017 achieved the policy “win-win”: revenue increased, and the affordability of cigarettes was reduced. The moderate tax increases in previous years were beneficial from the revenue perspective but had less impact on public health. However, the excise tax on tobacco products, and especially on non-filtered cigarettes, is still low compared to Georgia’s neighbor, Turkey, or to the EU. The excise tax was supposed to increase in January 2018, but the government planned to adopt a strong tobacco control bill in May of that year and decided to postpone the tax increase. It is also possible that the tobacco industry played a role in this decision, as it continues to influence government agencies and their officials. Further tax increases are urgently needed, since the affordability of the largest cigarette market segment increased from 2010 to 2017.

The recent changes in the tobacco control law are in line with Georgia’s commitments under the FCTC and under the 2014 Association Agreement calling for a gradual approximation of Georgia’s national legislation with the tobacco control legislation of the European Union (2014). Four main tobacco control measures hold greatest promise for Georgia: regular tax increases, smoke-free policy, advertising bans, and labeling/packaging rules. If Georgia implements these measures aggressively and durably, the country could avoid 3.6 billion GEL (1.5 billion USD) in economic losses caused by tobacco use over the next 15 years, obtaining a return on investment of 357 GEL (143 USD) for every 1 GEL invested (UNDP, 2018). The tobacco industry in Georgia is engaging in at least two forms of tax avoidance: forestalling and exploiting the tax difference between filtered and non-filtered cigarettes. This can be addressed by changing the tax law according to the international best practice (e.g., taxing existing inventories at the new tax rate once it becomes applicable) and by equalizing the tax rate for filtered and non-filtered cigarettes.

Recommendations

Tackle forestalling. There are many ways to deal with forestalling by industry. Many countries apply the new tax rate on all existing inventory by, for example, applying an additional tax stamp. Other countries prevent sale of cigarettes with old tax stamps within days after a tax increase. In the UK, for example, the tobacco companies cannot order tax stamps in excess of their average sales prior to a tax increase. Adopting anti-forestalling measures would lead to gains in tax revenue.

Rapidly align with the Protocol and the EU system. The government should analyze the extent to which its current system is compliant with the ITP and the EU track-and-trace system to be introduced in 2019. The ITP, for example, requires licensing of economic operators involved in the tobacco product supply chain. Georgia should, therefore, reinstitute

the licensing requirement, at least for cigarette manufacturers, importers, and exporters. Licensing requiring background checks would further aid enforcement. The ITP also requires marking of all tobacco products, including those intended for export. This, together with regular exchange of enforcement data with other countries, would enhance Georgia's contribution to the global effort to control international illicit trade in tobacco products. In this regard, Georgia should ratify the ITP. The effort needed to comply with the ITP would be minimal, since Georgia already meets most of the ITP requirements.

Reinforce international cooperation. Georgia should consider strengthening cooperation and information exchange with EU Member States, especially with those bordering Russia (e.g., Poland, Estonia, Lithuania), since they are facing similar illicit trade problems, and with its neighboring countries. Georgia can enhance its interaction with Interpol, the European Anti-Fraud Office (OLAF), and other relevant agencies in the fight against illicit tobacco trade.

Reinforce border protections and product movement control systems. Georgia should enhance the protection of its vulnerable border with Abkhazia and Ossetia by video monitoring of all trucks entering and leaving the country from those territories. Such a surveillance system could be supported by road cameras and mobile X-rays, and integrated with the e-Transport and the excise marking electronic system. Further, a system resembling the EU's Excise Movement and Control System (EMCS) or the Monitoring System for the Road Carriage of Goods (MSRCG) implemented recently in Poland should be considered, given the trade flows and the Agreement with the EU. These systems assist risk assessment and information exchange across relevant stakeholders. The MSRCG, for example, requires that all parties to a transaction involving transport of "sensitive goods" such as fuels, alcohol, and tobacco products (i.e., the sending entity, the receiving entity, the carrier and the driver) notify the Customs service authorities in advance about the movement of the goods.

Ensure that legislation adequately supports enforcement actions. To enhance compliance, Georgia should revisit its anticorruption laws, the criminal code, the codes of conduct, and the conflict of interest regulations so that they support the enforcement efforts of the Georgia Customs Services and the National Revenue Agency.

Accelerate plain packaging. The implementation of plain packaging, planned for December 31, 2022, could be speeded up. Even though the industry is pointing to a threat of illicit trade, there is no research evidence to justify such concerns (Evans and Reeves, 2015; Joossens, 2012; Scollo et al., 2014). Plain packaging could help to reduce the high smoking prevalence and in fact make identification of illicit cigarettes from other countries easier (Brennan et al., 2015; Durkin et al., 2015; Scollo et al., 2015; Wakefield et al., 2015).

Bring government-tobacco industry relations in line with international norms.

Government should amend its legislation to comply with Article 5.3 of the FCTC regarding tobacco-industry interference in policy making. The most relevant provisions for controlling the illicit tobacco market are requirements that the tobacco industry and/or its affiliates cannot be involved in discussions related to the ITP ratification or a track-and-trace system.

The administrative effort to control illicit trade in tobacco products should be supported by enhanced monitoring, a comprehensive surveillance system, and data analysis, so that policy making is backed up by solid research evidence and does not have to rely on data generated by the tobacco industry.

References:

- Academy of the Ministry of Finance. 2013. Retrieved from: <http://mofacademy.ge/News/2278>
- Bakhturidze GB, Ross H. What J, et al. 2008. Population survey on tobacco economy and policy in Georgia. FCTC Implementation and Monitoring Center in Georgia. 4-22.
- Bakhturidze G, Peikrshvili N, Mittelmark M. 2016. The influence of public opinion on tobacco control policy-making in Georgia: Perspectives of governmental and non-governmental stakeholders. *Tob. Prev. Cessation*; 2(January):1 DOI: www.dx.doi.org/10.18332/tpc/61580
- Border Police of Georgia, letter dated February 7, 2017, N MIA 2 18 00303660
- Brennan E, Durkin S, Coomber K. 2015. Are quitting-related cognitions and behaviours predicted by proximal responses to plain packaging with larger health warnings? Findings from a national cohort study with Australian adult smokers. *Tob Control*. 24. suppl 2.
- Ciecierski C, Chaloupka F. 2002. Data for Economic Analysis. World Bank.
- Commersant 2017 – I: http://commersant.ge/?view=post&id=133241&lang_id=en
- Commersant 2017-II: http://commersant.ge/?view=post&id=136599&lang_id=en
- Departments of Statistics of the Ministry of Economic Development of Georgia. 2006. Import-Export of Raw Tobacco in 2000-2004.
- Daily Sabah, Sep 25, 2015. Cigarette smuggling biggest source of income for PKK. Retrieved from: <https://www.dailysabah.com/investigations/2015/09/26/cigarette-smuggling-biggest-source-of-income-for-pkk>
- Durkin S, Brennan E, Coomber K, et al. 2015. Short-term changes in quitting-related cognitions and behaviours after the implementation of plain packaging with larger health warnings: findings from a national cohort study with Australian adult smokers. *Tob Control*. 24. suppl 2.
- EU-Georgia association Agreement 2014: Information is available at: <http://www.parliament.ge/ge/ajax/downloadFile/34753/AA> Or <https://www.matsne.gov.ge/ka/document/download/2496959/0/ge/pdf>
- Eurasianet, Apr 11, 2014. Georgia Feeds Turkey's Jones for Tobacco. By Nicholas Alan Clayton. Retrieved from: <https://eurasianet.org/node/68264>
- Euromonitor International. Cigarettes – Georgia. 2009, 2011, and 2017.

Evans-Reeves KA. Hatchard JL and Gilmore AB. 2015. 'It will harm business and increase illicit trade': an evaluation of the relevance, quality and transparency of evidence submitted by transnational tobacco companies to the UK consultation on standardised packaging 2012. *Tob Control*. 24(e2): e168-e177. doi: 10.1136/tobaccocontrol-2014-051930

Georgian Law on Tobacco Control, different versions incorporated in one. Retrieved in 2018 from: <https://matsne.gov.ge/ka/document/view/1160150>

Georgian Law on advertisement, different changes incorporated in one. Retrieved from: <https://matsne.gov.ge/ka/document/view/31840>

Georgian Tax Code, 2018. Changes made during 2000-2017. Edition 1997-2004 retrieved from: <https://matsne.gov.ge/ka/document/view/31690>

Edition 2004-2010 Retrieved from: <https://matsne.gov.ge/ka/document/view/32842>

Edition after 2010. retrieved from: <https://matsne.gov.ge/ka/document/view/1043717>

Geostat – National Statistics Office of Georgia, letters dated: January 25, 2018, N 5-182; March 9, 2018, N 10-638; April 12, 2018, N 5-1021.

Gilmore A., Pomerleau J., McKee M., Rose R., Haerpfer C., Rotman D., Tumanov S. et al. 2004. Prevalence of Smoking in 8 Countries of the Former Soviet Union: Results from the Living Conditions, Lifestyles and Health Study. *American Journal of Public Health*. 94(12). 2177-87.

Hurriyetarynews May 14, 2015. Cigarettes smuggled from Georgia, Northern Iraq, Bulgaria. Retrieved from: <http://www.hurriyetarynews.com/cigarettes-smuggled-from-georgia-northern-iraq-bulgaria-82431>

Institute of Social Studies and Analysis (ISSA). 2016. Public Attitudes regarding tobacco control policy in Georgia. Retrieved from: <http://issa-georgia.com/ge/non-entrepreneurial-non-commercial-legal-entity/tabaqos-kontrolis-charcho-konventsiiis-implementatsiisa-da-monitoringis-tsentri/10>

Investigation Service of Ministry of Finance of Georgia, letter dated February 5, 2018; N 924/15-02

Joossens L. 2012. Smuggling the tobacco industry and plain packs. *Cancer Research UK*. https://www.cancerresearchuk.org/sites/default/files/smuggling_fullreport.pdf

Kobeshavidze, Meskhishvili, Bakhturidze, Grigalashvili. 2003. Cigarette smuggling and illicit trade problems in Georgia. Georgian National Counter Tobacco Center. Tbilisi.

Krasovsky. KS. 2013. The impact of changes in excise rates on the cigarette market and budget revenues in Georgia (unpublished manuscript in Russian).

Law on Advertisement of Georgia. 2009. Retrieved from: <https://matsne.gov.ge/ka/document/view/31840>

Law on food and tobacco. 2010. Retrieved from: <https://matsne.gov.ge/ka/document/view/11938>

Law on Licensing and Permissions 2005. Retrieved from: <https://matsne.gov.ge/ka/document/view/26824>

Ministry of Interior Affairs, letter dated January 23, 2018, N MIA 1 18 00172449

Ministry of Finance 2017 See the prices respectively for 2017 and 2018 at <https://mof.ge/images/File/sajaro.../410/gamosaqveynebeli.xlsx>
<https://mof.ge/images/File/kanonmdebloba/brz-277-danarti.xlsx>

Ministry of Finance 2018, web site: <https://mof.ge/en/>

Confronting Illicit Tobacco Trade: A Global Review of Country Experiences

- National Statistics Office of Georgia. Statistical Yearbooks of Georgia. 2005-2017.
- Omega group tobacco (OGT): <https://ogt.ge/en/invention-cigarette-mouthpiece/>
- Panorama, Aug 5, 2015. Turkey seizes 3.5 million packets of cigarettes smuggled from Georgia. Retrieved from: <https://www.panorama.am/en/news/2015/08/05/turkey-georgia/1212>
- Eurasianet 2014: <https://eurasianet.org/node/68264>
- Revenue service of Georgia, MoF web site info updated in June 5. 2012: http://rs.ge/Default.aspx?sec_id=4816&lang=2
- Revenue service of Georgia, MoF web site info updated in March 11. 2015: www.rs.ge/en/5253
- Revenue service of Georgia, MoF web site info updated in 2018: http://www.rs.ge/Default.aspx?sec_id=5405&lang=2&catid=69
- Scollo M, Bayly M and Wakefield M. 2014. Availability of illicit tobacco in small retail outlets before and after the implementation of Australian plain packaging. *BMJ* Vol. 24.e1.
- Scollo M., Zacher M., Coomber K., Wakefield M. 2015. Use of illicit tobacco following introduction of standardised packaging of tobacco products in Australia: results from a national cross-sectional survey. *Tob Control*. 24. suppl 2.
- Shalutashvili A, Ross H, Watt J, Hilborn S, Bakhturidze G, Kobeshavidze G, Grigalashvili Z. 2007. Tobacco Economic Study in Georgia since the fall of the Soviet Union. FCTC Implementation and Monitoring Center in Georgia.
- SICPA web site: <https://www.sicpa.com/offices/georgia-tbilisi>
- Sputnik-Georgia 2017. Retrieved from: <https://sputnik-georgia.ru/incidents/20171031/237985553/Sigarety-vmesto-kamnej-i-cvetovgrazhdane-Armenii-popalis-v-Gruzii.html>
- State Department of Statistics. 2004. Retrieved from: <http://www.geostat.ge/index.php?action=search&lang=eng>
- STEPS Survey for Georgia. 2016. Retrieved from: http://ncdc.ge/AttachedFiles/STEPS%20report%20full-final_51403d9f-eda5-4789-93e0-3466d2711e17.pdf
- Petraishvili V, Shamugia N, Bakhturidze G, Gvinianidze K, Goginashvi K, Archvadze I, Moroshkina N, Maglakelidze N, Tesche J, Wood L. 2016. Tobacco Products Taxation Policy (Georgia). National Center for Disease Control on Georgia. Ministry of Labor, Health and Social Affairs of Georgia.
- UNDP, National Center for Diseases Control and Public Health of Georgia (NCDC); RTI International, WHO FCTC Secretariat. 2018. The case for investing in WHO FCTC implementation in Georgia. See report at: <http://www.ncdc.ge/Pages/User/News.aspx?ID=5aada9ce-57aa-4ec5-9d81-915d43c388e9>
- Wakefield M, Coomber K, Zacher M, et al. 2015. Australian adult smokers' responses to plain packaging with larger graphic health warnings 1 year after implementation: results from a national cross-sectional tracking survey. *Tob Control*. 24. suppl 2.
- WHO (World Health Organization). 2012. The Protocol to Eliminate Illicit Trade in Tobacco Products. <http://www.who.int/fctc/protocol/en/>
- WHO (World Health Organization). 2015. MPOWER: See information at: http://www.who.int/tobacco/global_report/2015/en/

WHO (World Health Organization). Framework Convention on Tobacco Control (FCTC) text: retrieved from: [www.fctc.org.ge](http://www.fctc.org/ge)

WHO Global Tobacco Control Report. 2017. Monitoring tobacco use and prevention. Retrieved from: <http://apps.who.int/iris/bitstream/handle/10665/255874/9789241512824-eng.pdf;jsessionid=3CDB6F426A1DD0F8BBF0E05359E200F1?sequence=1>

World Bank. 1996. "Reforms in Food and Agriculture in Georgia". Washington, DC: World Bank.

COVER QUOTE SOURCES

ⁱ WHO Framework Convention on Tobacco Control Press Release, June 28, 2018.
<https://www.who.int/fctc/mediacentre/press-release/protocol-entering-into-force/en/>

ⁱⁱ World Health Organization Press Release, July 19, 2017.
<https://www.who.int/en/news-room/detail/19-07-2017-who-report-finds-dramatic-increase-in-life-saving-tobacco-control-policies-in-last-decade>

ⁱⁱⁱ Combatting illicit trade in tobacco products: Commissioner Andriukaitis' Statement on the EU's adoption of an EU-wide track and trace system. European Commission Press Release, December 15, 2017.
http://europa.eu/rapid/press-release_STATEMENT-17-5269_en.htm

^{iv} How to design and enforce tobacco excises? International Monetary Fund, October 2016
<https://www.imf.org/en/Publications/Fiscal-Affairs-Department-How-To-Notes/Issues/2016/12/31/How-to-Design-and-Enforce-Tobacco-Excises-44352>

^v World Bank Group: "Global Tobacco Control: A Development Priority for the World Bank Group", Preface of WHO Global Tobacco Report 2015.
http://www.who.int/tobacco/global_report/2015/timevansandworldbankforeword.pdf?ua=1

“To tackle illicit trade is to tackle accessibility and affordability of tobacco products, to be more effective on the control of the packaging and to reduce funding of transnational criminal activities whilst protecting the governmental revenues from tobacco taxation.”ⁱ

– **Dr. Vera Luiza da Costa e Silva**
Head of the Secretariat of the WHO Framework Convention on Tobacco Control

“Governments around the world must waste no time in incorporating all the provisions of the WHO Framework Convention on Tobacco Control into their national tobacco control programmes and policies. They must also clamp down on the illicit tobacco trade, which is exacerbating the global tobacco epidemic and its related health and socio-economic consequences.”ⁱⁱ

– **Dr. Tedros Adhanom Ghebreyesus, Director-General**
World Health Organization

“Tobacco still remains the biggest avoidable cause of premature death in the EU, and the illicit trade in tobacco facilitates access to cigarettes and other tobacco products, including for children and young adults. In addition, millions of euros in tax revenues are lost every year as a result of the illicit trade.”ⁱⁱⁱ

– **Commissioner Vytenis Andriukaitis**
Health and Food Safety / European Commission

“Given their light weight, small size, and high value, tobacco products are susceptible to fraud through illegal trade, production, and cultivation. . . . Illegal trade is a context-specific activity that has various modus operandi and therefore requires multi-dimensional context-specific solutions.”^{vi}

– **Patrick Petit (Senior Economist) & Janos Nagy (Senior Economist)**
Fiscal Affairs Department / International Monetary Fund

“Effective tobacco tax regimens that make tobacco products unaffordable represent a 21st century intervention to tackle the growing burden of noncommunicable diseases. We are convinced that, working together with WHO and other partners in support of countries, we will be able to prevent the human tragedy of tobacco-related illness and death, and save countless lives each year.”^v

–**Dr. Tim Evans (Senior Director) & Patricio V Márquez (Lead Public Health Specialist)**
Health, Nutrition and Population Global Practice / World Bank Group

