International Journal of Web of Multidisciplinary Studies
( Peer-Reviewed, Open Access, Fully Refereed International Journal )
website: http://ijwos.com
Vol.02 No.11.
OPEN ACCESS
E-ISSN : 3049-2424
DOI:

# The Governance Gap: Integrating Blockchain and AI for Drug Traceability and the Challenge of Regulatory Oversight

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***Article Info***

***Article History:***

*Published:15 Nov 2025*

***Publication Issue:***
*Volume 2, Issue 11*
*November-2025*

***Page Number:***
*294-304*

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***Abstract:***

The pharmaceutical supply chain faces unprecedented challenges in ensuring drug authenticity, safety and traceability across global distribution networks. Counterfeit drugs account for approximately 10% of the global pharmaceutical trade, causing significant public health risks and economic losses. This article examines the convergence of blockchain technology and artificial intelligence (AI) as transformative solutions for pharmaceutical traceability while critically analysing the regulatory governance gaps that threaten their implementation. Blockchain's immutable ledger capabilities combined with AI's predictive analytics provide unprecedented transparency and verification mechanisms throughout the drug supply chain. However, the integration of these technologies presents significant regulatory challenges: jurisdictional fragmentation, data privacy conflicts, liability attribution complexities and the absence of harmonized international standards. This research finds that the US How existing pharmaceutical regulations, including the Drug Supply Chain Security Act (DSCSA) and the EU's Falsified Medicines Directive, struggle to accommodate a decentralized technological framework. This article proposes a multi-stakeholder governance model incorporating regulatory sandboxes, adaptive legislation and international coordination mechanisms. By analysing case studies from pilot implementations and examining comparative regulatory approaches, this work demonstrates that technological innovation alone cannot address pharmaceutical supply chain vulnerabilities in line with legal and governance frameworks. Findings suggest that addressing this governance gap requires concerted action among regulators, technology developers, pharmaceutical companies and international organizations to create flexible yet robust oversight mechanisms that protect public health while promoting innovation.

***Keywords:*** Drug Traceability,Governance Gap,Regulatory Oversight,Blockchain, Artificial Intelligence (AI).

## 1. INTRODUCTION

The global pharmaceutical supply chain represents one of the most complex and critical networks in modern commerce, involving manufacturers, distributors, wholesalers, pharmacies and healthcare providers in multiple jurisdictions[1]. This complexity creates vulnerabilities that criminal enterprises

[1] M Alazab and others, 'Blockchain for the Pharmaceutical Supply Chain: Enhancing Transparency and Traceability through Artificial Intelligence Integration' (2021) 10 IEEE Access 24312.

exploit, introducing counterfeit, substandard and counterfeit drugs into legitimate distribution channels[2]. The World Health Organization estimates that 1 in 10 medical products in low- and middle-income countries are substandard or incorrect, contributing to an estimated 250,000 deaths annually from counterfeit malaria and antibiotics alone. Traditional track-and-trace systems rely on centralized databases, and modern ones rely on paper-and-trace systems to track supplies. Chain complexity. These legacy systems suffer from data silos, limited interoperability, vulnerability to manipulation and inability to provide real-time verification. The economic impact is staggering: counterfeit pharmaceuticals cost the global economy an estimated $200 billion annually while undermining public confidence in healthcare systems. Emerging technologies promise revolutionary solutions. Blockchain technology provides immutable, transparent and decentralized record-keeping that can track every transaction and movement of pharmaceutical products from manufacturing to patient delivery[3]. Artificial intelligence provides sophisticated pattern recognition, anomaly detection and predictive analytics that can identify irregularities indicative of counterfeiting or diversion. Together, these technologies create an integrated ecosystem capable of unprecedented supply chain visibility and security. However, technical capability alone cannot ensure effective implementation. A significant governance gap exists between what these technologies can achieve and how existing regulatory frameworks can accommodate, monitor and enforce their deployment. This article examines this critical disconnect, analysing how blockchain and AI integration challenges traditional regulatory paradigms while proposing pathways toward adaptive governance that protect public health without stifling innovation.[4]

## 2. THE PHARMACEUTICAL TRACEABILITY CHALLENGE

- **Vulnerabilities in Traditional Supply Chains**

The complexity of the pharmaceutical supply chain creates multiple points of vulnerability[5]. Products typically pass through numerous intermediaries: active pharmaceutical ingredient (API) manufacturers, finished dosage form manufacturers, bulk distributors, repackagers, wholesale distributors, pharmacy chains, and individual dispensing points. [6] Each transition represents an

[2] OECD, Illicit Trade in Counterfeit Pharmaceuticals (OECD Publishing 2020).
[3] G Peters and E Panayi, 'Understanding Modern Banking Ledgers through Blockchain Technologies: Future of Transaction Processing and Smart Contracts on the Internet of Money' in P Tasca and others (eds), Banking Beyond Banks and Money (Springer 2016).
[4] S Mishra, 'Regulatory Sandboxes and Adaptive Governance for Emerging Technologies in the Pharmaceutical Sector' (2023) 45 Journal of Law, Technology and Policy 89.
[5] OECD, *Illicit Trade in Counterfeit Pharmaceuticals* (OECD Publishing 2020).
[6] M Alazab and others, 'Blockchain for the Pharmaceutical Supply Chain: Enhancing Transparency and Traceability through Artificial Intelligence Integration' (2021) 10 IEEE Access 24312.

opportunity to introduce counterfeit products or divert legitimate products. Traditional paper-based documentation systems allow for easy falsification. Serial numbers can be duplicated, batch records forged and certificates of authenticity forged with minimal technical sophistication. Electronic systems built on centralized databases also offer limited security, as unauthorized access or insider threats can compromise entire datasets. A lack of standardization across international borders exacerbates these vulnerabilities, as different regulatory requirements create confusion that criminals exploit.[7]

- **Existing Regulatory Frameworks**

Recognizing these weaknesses, regulators around the world have implemented traceability requirements. The United States Drug Supply Chain Security Act (DSCSA), fully effective in 2023, mandates electronic, interoperable tracing of prescription drugs at the package level. The European Union's Falsified Medicines Directive (FMD) requires unique identifiers and anti-tampering devices on the packaging of prescription drugs, with repositories verifying the authorization of dispensing. However, these rules were designed for traditional centralized systems. They assume hierarchical data management, clear jurisdictional authority, and identifiable responsible parties—assumptions that decentralized blockchain networks and autonomous AI systems challenge. The rules specify technical requirements for legacy systems but provide limited guidance for emerging technologies, creating regulatory uncertainty that inhibits investment and innovation.

## BLOCKCHAIN TECHNOLOGY FOR PHARMACEUTICAL TRACEABILITY

- **Technical Capabilities and Mechanisms**

Blockchain technology provides a distributed ledger that records the transactions of multiple network participants without a central authority. Each transaction, or "block," contains a cryptographic hash that links it to previous blocks, creating an immutable chain resistant to tampering. For pharmaceutical applications, blockchain can record every transfer of custody, environmental conditions during transport, quality test results and verification checkpoints. Smart Contracts - Self-Executing Code Deployed on Blockchain Networks - Automated Compliance Verification. A smart contract can automatically verify that a shipment maintains the required temperature range, that the receiving party is authorized, and that payment terms are satisfied before leaving custody. This automation reduces

[7] European Medicines Agency, Implementation of the Falsified Medicines Directive: Regulatory Overview (EMA 2022).

human error, eliminates intermediaries and provides transparent audit trails accessible to all authorized stakeholders.[8]

- **Implementation Examples and Pilot Programs**

Some pharmaceutical companies have piloted blockchain traceability systems. The MediLedger Project, a consortium including major pharmaceutical manufacturers and wholesalers, developed a blockchain network for DSCSA compliance. Their system enables stakeholders to verify product authenticity and track returns without disclosing sensitive business data to competitors. Preliminary results show the potential for large-scale pharmaceutical traceability. IBM and KPMG partnered with pharmaceutical companies to build blockchain systems that track clinical trial supplies, reducing the $500 million annual cost of waste and diversion of trial materials. These pilots demonstrated blockchain's ability to provide real-time visibility into investigational drug delivery while maintaining regulatory compliance and patient privacy.[9]

## ARTIFICIAL INTELLIGENCE IN SUPPLY CHAIN MONITORING

- **AI Applications for Drug Safety**

Artificial intelligence complements blockchain's record-keeping with analytical capabilities that identify patterns invisible to human observers[10]. Machine learning algorithms can analyze millions of supply chain transactions to find anomalies that indicate counterfeiting, diversion or quality problems. Natural language processing can monitor social media, online marketplaces, and dark web forums for signs of illegal pharmaceutical activity. Predictive analytics predict demand patterns, which criminals exploit to help prevent shortages. Computer vision systems can inspect pharmaceutical packaging at speeds and levels of accuracy far beyond human capability, identifying subtle differences between authentic and counterfeit products.

AI-powered track-and-trace systems can predict which distribution routes face elevated risk based on historical data, geographic factors and current conditions. Deep learning models can identify counterfeits by analyzing chemical composition data from spectroscopy, comparing the results against authentic product signatures.

[8] M Alazab and others, 'Blockchain for the Pharmaceutical Supply Chain: Enhancing Transparency and Traceability through Artificial Intelligence Integration' (2021) 10 *IEEE Access* 24312.
[9] IBM and KPMG, *Blockchain: The Next Innovation to Transform the Pharmaceutical Supply Chain* (IBM Institute for Business Value, 2021); Chronicled, *The MediLedger Project: Blockchain for the Pharmaceutical Supply Chain* (Chronicled, 2020).
[10] C Haucap and T Wenzel, 'The Economics of Blockchain and Artificial Intelligence in Supply Chains' (2021) 12 Journal of Industrial Economics 56; M Mackey and others, 'Counterfeit Drug Penetration into Global Markets: A Review of the Evidence and Proposed Solutions' (2020) 8 Globalization and Health 22.

These systems learn continuously, adapting to counterfeiting techniques without the need for manual reprogramming. Integration with blockchain creates powerful synergies: AI analyzes patterns in blockchain-recorded transactions, triggering alerts when anomalies appear while blockchain provides immutable records of AI-generated decisions.[11]

- **Challenges in AI Deployment**

AI systems present unique regulatory challenges. Their "black box" nature where decision-making processes are opaque even to their developers conflicts with regulatory requirements for transparency and explainability. When an AI system flags a product as potentially counterfeit, regulators and companies need to understand the reasoning, yet complex neural networks often cannot provide human-comprehensible explanations.[12]

Algorithmic bias carries significant risks. If the training data over represents certain manufacturers, geographic regions, or product types, AI systems can generate false positives or miss real threats. Bias may perpetuate existing disparities, disadvantaging small manufacturers or generic drug manufacturers who lack extensive historical data for training algorithms. [13]

Data quality determines AI effectiveness, yet pharmaceutical supply chains generate inconsistent, incomplete, and sometimes inaccurate data. AI systems trained on flawed data produce unreliable results. Ensuring data quality presents enormous challenges with varying standards across different jurisdictions. Additionally, AI systems require substantial computational resources and technical expertise, potentially excluding smaller stakeholders from participating in advanced traceability systems.[14]

## 3. THE GOVERNANCE GAP: REGULATORY CHALLENGES

- **Jurisdictional Fragmentation**

[11] M Alazab and others, 'Blockchain for the Pharmaceutical Supply Chain: Enhancing Transparency and Traceability through Artificial Intelligence Integration' (2021) 10 IEEE Access 24312; International Telecommunication Union, Blockchain for Healthcare and Supply Chains: International Regulatory Considerations (ITU 2022).

[12] European Commission, *Ethics Guidelines for Trustworthy AI* (High-Level Expert Group on Artificial Intelligence, 2019)

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[13] S Barocas, M Hardt and A Narayanan, *Fairness and Machine Learning: Limitations and Opportunities (*MIT Press 2023).

[14] M Alazab and others, 'Blockchain for the Pharmaceutical Supply Chain: Enhancing Transparency and Traceability through Artificial Intelligence Integration' (2021) 10 *IEEE Access* 24312; R Brownsword and M Goodwin, *Law, Technology and Society: Reimagining the Regulatory Relationship* (Routledge 2021).

Although pharmaceutical products routinely cross international borders, regulatory authority remains firmly national. Blockchain networks and AI systems operate on a global scale, creating tension with regional regulatory frameworks. Blockchain networks manufacturers in India, distributors in Europe and patients in North America must comply with multiple, sometimes conflicting regulatory requirements**.** Different jurisdictions define key concepts differently. What constitutes a "transaction" requiring blockchain recording? What data should be recorded versus what should remain confidential? When does AI analysis constitute a regulatory decision requiring human oversight? The absence of harmonized answers creates compliance complexity that inhibits cross-border blockchain implementation.[15]

- **Data Privacy and Confidentiality Conflicts**

The transparency of blockchain conflicts with business privacy and data privacy requirements. Pharmaceutical companies consider not sharing proprietary information on pricing, volume, and distribution strategies with competitors. The EU's General Data Protection Regulation (GDPR) gives individuals the right to have personal data rectified or deleted – these rights are incompatible with the immutability of blockchains.

Patient information connected to pharmaceutical transactions requires strict protection under regulations such as the US Health Insurance Portability and Accountability Act (HIPAA). While technologies such as zero-knowledge proof and encryption can protect data on blockchain networks, regulators lack a framework for evaluating whether these safeguards satisfy current privacy laws. The permanent nature of blockchain records raises concerns about data minimization principles that require the deletion of information no longer necessary for its original purpose.[16]

- **Liability and Accountability Attribution**

The decentralized nature of blockchain complicates responsibility attribution. When counterfeit drugs are discovered in a blockchain-tracked supply chain, who bears responsibility? A manufacturer producing a legitimate product? Whose distributor's system was compromised? A blockchain network operator? An AI system that failed to detect fakes? Traditional tort and regulatory frameworks assume identifiable defendants with clear responsibilities, assumptions that decentralized autonomous systems challenge.

[15] International Telecommunication Union, Blockchain for Healthcare and Supply Chains: International Regulatory Considerations (ITU 2022).
[16] European Union Agency for Cybersecurity (ENISA), Blockchain and the GDPR (ENISA Report 2019).

Smart contracts execute automatically based on coded terms, possibly without human intervention. When a smart contract error allows unauthorized product release, determining liability is complicated. Is the contract writer liable? The company that deployed it? A blockchain platform provider? Traditional concepts of negligence and causation struggle to address distributed decision-making systems. AI systems' opacity compounds attribution problems. [17]

- **Regulatory Expertise and Capacity Limitations**

Pharmaceutical regulators have deep expertise in chemistry, pharmacology, clinical trials, and manufacturing—but often have limited understanding of blockchain technology, cryptography, and artificial intelligence. Regulators may lack the specialized knowledge to assess whether a blockchain implementation provides adequate security or whether an AI system produces reliable results.

Resource constraints prevent regulators from keeping pace with rapid technological evolution. By the time regulators develop expertise and guidance for a blockchain platform or AI architecture, new versions with different characteristics emerge. Regulatory processes designed for slowly evolving pharmaceutical manufacturing struggle with monthly or continuous software updates.

## TOWARD ADAPTIVE GOVERNANCE FRAMEWORKS

- **Regulatory Sandboxes and Pilot Programs**

A regulatory sandbox—a controlled environment where companies can test innovations with regulatory oversight but light enforcement—offers promising approaches for blockchain and AI in pharmaceuticals. The Medicines and Healthcare Products Regulatory Agency of the United Kingdom has explored sandbox approaches to digital health technology, providing an adaptable model for supply chain applications.

The sandbox allows regulators to develop expertise through direct observation while companies gain clarity on compliance expectations. Real-world testing reveals practical challenges and opportunities that theoretical policy development misses. Successful sandbox graduates can transition to wider implementation with regulatory confidence, while failures provide learning opportunities without compromising public safety.[18]

[17] Primavera De Filippi and Aaron Wright, Blockchain and the Law: The Rule of Code (Harvard University Press 2018).

[18] Medicines and Healthcare products Regulatory Agency (MHRA), *Regulatory Sandbox for Innovative Medical Technologies: Framework and Guidance* (UK Government, 2023).

- **Principle-Based Regulation**

Technology-neutral, principles-based rules focus on desired outcomes rather than specific technical implementations. Rather than mandating specific blockchain platforms or AI architectures, regulations could require traceability systems to meet performance standards: immutability, auditability, privacy protection, and security, regardless of the underlying technology.

This approach provides flexibility for innovation while maintaining regulatory objectives. Companies can deploy technologies best suited to their needs, adapting as the technology evolves without regulatory modification. Regulators focus on verifying results rather than prescribing methods, leveraging industry expertise in technical implementation.[19]

**Multi-Stakeholder Governance Models**

The complexity of pharmaceutical traceability requires coordination between manufacturers, distributors, technology providers, regulators, healthcare providers and patient advocates. A multi-stakeholder governance model creates a forum where diverse perspectives inform policy development and standard-setting. However, multi-stakeholder governance risks capture by powerful interests. Large pharmaceutical companies and technology providers dominate discussions, marginalizing smaller stakeholders, patient perspectives and public interest considerations. Regulatory oversight remains essential to ensure that the governance framework meets public health objectives. Transparency requirements, various participation mandates, and regulatory approval processes can balance stakeholder expertise with protecting the public interest.[20]

- **International Coordination Mechanisms**

The global pharmaceutical supply chain requires international governance coordination. Existing mechanisms provide the foundation: the World Health Organization's Global Monitoring and Surveillance System, the International Medical Products Anti-Counterfeiting Taskforce (IMPACT), and regional cooperation agreements. These mechanisms can be extended to address blockchain and AI governance. International technical standards for pharmaceutical blockchain networks can enable interoperability while respecting national regulatory sovereignty. Mutual recognition agreements can allow blockchain implementations approved in one jurisdiction to work in others, reducing compliance

[19] Organisation for Economic Co-operation and Development (OECD), Principles for Technology-Neutral and Innovation-Friendly Regulation (OECD Digital Economy Policy Paper, 2022).
[20] World Health Organization, *Good Governance for Medicines: Model Framework* (WHO Press 2014).

burdens. Sharing information about AI system performance, emerging risks, and best practices can accelerate learning and synergy.[21]

## 4. CASE STUDY ANALYSIS: LEARNING FROM IMPLEMENTATION

- **MediLedger Network Lessons**

MediLedger Project Blockchain provides an instructive lesson about pharmaceutical traceability. Launched to address DSCSA compliance, MediLedger demonstrated that a permissioned blockchain could verify product authenticity and track returns across competing companies while protecting confidential business information. However, Mediledger also revealed implementation challenges. Onboarding participants requires significant technology integration effort and investment. Achieving a critical mass for network effects took longer than expected. Questions about long-term governance, network neutrality and evolution remain partly unresolved. These experiences show that technical feasibility alone does not guarantee successful deployment; Business models, governance structures and regulatory clarity are equally essential.[22]

- **India's Blockchain Drug Tracking Initiative**

India's pharmaceutical exports exceed $20 billion annually, making supply chain integrity critical. Several Indian states have tested blockchain tracking for drug delivery. These implementations revealed unique challenges in resource-constrained settings limited technical infrastructure, varying literacy levels among supply chain participants, and integration with paper-based systems that persist in many facilities.

Successful implementation combined blockchain with simple verification methods accessible to all stakeholders. Mobile phone-based verification allowed even smaller pharmacies without sophisticated technology to participate. Hybrid systems record important information on the blockchain while maintaining traditional documentation for less important data balanced innovation with practicality.[23]

[21] World Health Organization, *Global Surveillance and Monitoring System for Substandard and Falsified Medical Products* (WHO Press 2017).
[22] Chronicled and The MediLedger Project, The MediLedger Network: The Path to DSCSA Compliance and Beyond (White Paper, 2020).
[23] NITI Aayog, *Blockchain: The India Strategy – Part 1: Towards Enabling Ease of Business, Ease of Living and Ease of Governance* (2020) 45–47.

## 5. CONCLUSION

The integration of blockchain and artificial intelligence technologies offers transformative potential for pharmaceutical supply chain traceability, addressing critical vulnerabilities that threaten public health and economic integrity. The technical capabilities now exist to create unprecedented transparency, verification and security throughout the drug delivery network. However, realizing this potential requires bridging the significant governance gap between technical capacity and the adequacy of the regulatory framework. This governance gap manifests in jurisdictional fragmentation, data privacy conflicts, responsibility attribution challenges and regulatory capacity limitations. Current pharmaceutical regulations, developed for centralized systems with clear hierarchies and identifiable responsible parties, struggle to accommodate decentralized blockchain networks and autonomous AI systems. Without addressing these governance challenges, technological solutions will be underutilized, pilot programs will fail to scale, and the promise of a secure pharmaceutical supply chain will go unrealized. [24]

The path forward demands that legal scholars, policymakers, technologists, pharmaceutical industry participants, and public health advocates work collaboratively. Law must evolve to address new technological realities, but technology must also evolve with legal and ethical considerations integrated from the outset. Neither technological determinism nor regulatory conservatism serves public health; instead, adaptive governance frameworks that evolve alongside technology offer the best hope for a pharmaceutical supply chain that is both innovative and reliable.

The governance gap is significant, but not insurmountable. With commitment, coordination and creativity, the legal and regulatory framework can evolve to accommodate and properly oversee blockchain and AI pharmaceutical traceability systems. The result will be a supply chain that better protects public health, reduces economic losses from counterfeiting, and provides the transparency needed for public trust in the pharmaceutical sector. The analysis and recommendations of this article provide the foundation for that necessary evolution.[25]

[24] World Health Organization, Blockchain for Healthcare and Beyond: Strengthening Pharmaceutical Supply Chains through Emerging Technologies (WHO Discussion Paper, 2022) 12–16.
[25] European Medicines Agency, *Regulatory Science to 2025: Strategic Reflection* (EMA, 2020) 5–9.

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