

Illicit Tobacco

An introductory guide
for enforcement agencies



CONTENTS

| | |
|--|-----------|
| Introduction | 3 |
| What are illicit tobacco products? | 4 |
| Who buys illicit product? | 5 |
| The economic cost of illicit tobacco products | 6 |
| The impact on health | 6 |
| National strategies to tackle the problem | 7 |
| Enforcement agencies | 7 |
| Regional strategies | 7 |
| The legislation | 8 |
| Case studies and contacts | 10 |
| References | 14 |

Introduction

Price increases have been a highly successful way of helping people become non-smokers: UK budget changes to tobacco duty have saved lives and prevented much serious illness.

The UK has the most expensive cigarettes in the EU and among the most expensive cigarettes in the world. This is in large part to deter people from smoking.

However, the public health benefits of this taxation policy have been greatly undermined by tobacco smuggling.

Smuggled tobacco now accounts for about 17% of the tobacco market.

Increased smuggling leads to the wide availability of cheap cigarettes to the poorest people thereby maintaining high smoking rates among disadvantaged groups; and contributing significantly to widening health inequalities.

Counterfeit tobacco accounts for an increasing amount of smuggled tobacco in the UK.

Over 25% of smuggled tobacco is counterfeit, often manufactured in the Far East, and over half of all hand-rolled tobacco smoked in the UK.



Tackling health inequalities caused by smoking

Twenty-five councils in England¹ with areas of high smoking prevalence, leading to health inequalities, have benefited in 2009 from a partnership between the Department of Health and the LGA Group.

The "Reducing Health Inequalities through Tobacco control" programme, managed by IDeA, has aimed to help councils tackle smoking problems in their area through a variety of means, including capacity building and provision of information/assistance on effective ways to increase support for would be quitters amongst young people, routine and manual workers and those pregnant or likely to become pregnant.

Tackling illicit tobacco is one of the main areas of the programme and key elements identified by the councils included:

- tackling the supply of illegally imported tobacco, which is then sold to young people, and
- better enforcement action against the illegal sale of tobacco

In addition to this all council's trading standards services across England and Wales have participated in additional tobacco control work, including tackling underage sales, ensuring compliance with advertising controls and tackling illicit tobacco. This has been a separate fund provided by DH and administered by LACORS.



What are illicit tobacco products?

Illicit Tobacco

Illicit Tobacco is described as not having had the duty paid on it or it having been smuggled or illegally produced. The Tobacco Products Duty Act 1979² provides the provisions for paying duty on tobacco and tobacco products.

The UK tax on tobacco products including cigarettes, cigars and hand rolled tobacco is the highest in the European Union. Cheap and illicit tobacco undermines any work that the impact of taxation and other tobacco control measures put in place. Measures such as raising the age of sale to 18 and picture health warnings on packaging are rendered less effective whilst illicit tobacco exists.

The revenue loss from the supply of illicit tobacco in the UK ranged from:

£0.5 bn - £1.9bn for cigarettes and £0.5 bn - £0.75 bn for hand rolled tobacco in 2007-8.³

The current economic climate is believed to lead to an increase in the consumption of illicit tobacco as more smokers take advantage of cheaper products. Smuggling and counterfeiting of tobacco increase its availability with it being sold at less than half the tax-paid UK legitimate price.

There are three sources of illicit tobacco:

1. Smuggled product

This is usually part of large scale organised crime and involves the illegal transportation, distribution and sale of genuine tobacco products. This means that legitimately manufactured products are diverted through the supply chain and thus tax is evaded. Whilst the products are cheaper to the consumer there is still a profit to be made to the smugglers. Generally smuggled tobacco is transported in containers (by way of sea, road or rail) postal routes and with tourists. HMRC report that this accounts for 70-80% of illicit cigarette imports.

2. Bootlegging

This is a form of smuggling generally carried out by individuals ("white van man") or small gangs. The products are purchased from countries with low levels of taxation (generally EU or Eastern Europe / Russian countries) and brought back into the UK for distribution.

3. Counterfeiting

This refers to the illegal manufacture of tobacco products where the product bears the trademark without the consent of the owner of that trade mark. Typically, the tobacco products are made from inferior materials with the final product made to look genuine.

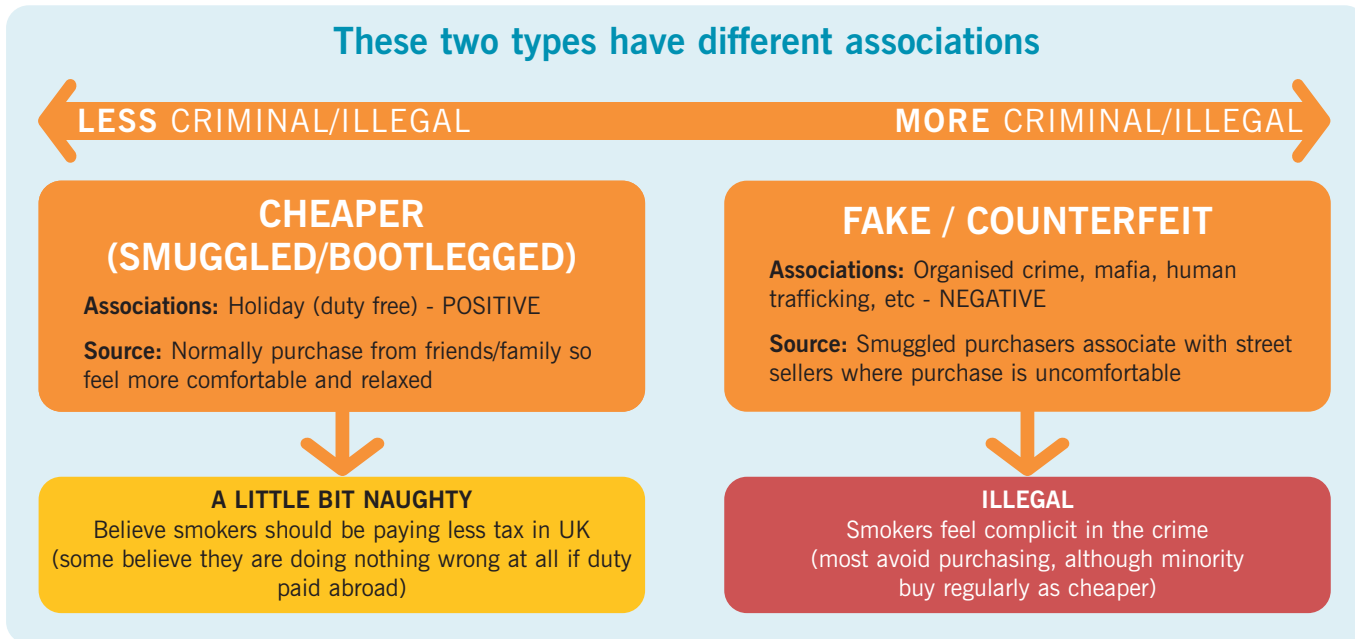
Most of the counterfeit product originates from Eastern Europe or East Asia; however it can also originate in the UK from tobacco rejected by tobacco manufacturers. These products are then distributed covertly and sold in order to evade taxation. In 2001/02 15% of the large seizures of cigarettes made by HMRC were counterfeit⁴, by 2007-8 this had risen to 51%⁵



Who buys illicit tobacco?

Research carried out in 2009 on behalf of Smokefree London⁶ by Directions Research Marketing reveals that it is routine and manual workers who are more likely to use illicit tobacco products.

Broadly speaking, this group recognised two main sources of illicit tobacco; “cheap” – referring to smuggled or bootlegged tobacco and counterfeit or “fake” products. There are very different attitudes displayed towards the products which will be used in the future to successfully target communication and actions.



North of England Illicit Tobacco Survey 2009

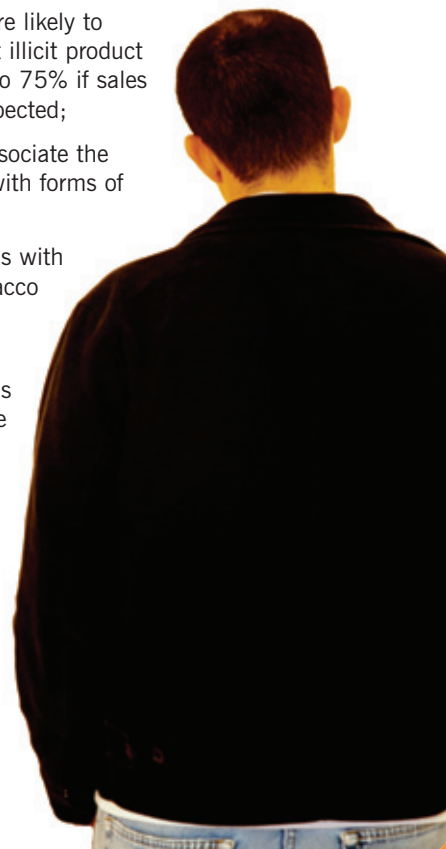
A large scale opinion and behaviour survey across the North of England was commissioned in 2009⁷. This included 6,000+ street and telephone interviews and data from all 49 trading standards areas. The information was collated to assist in audience segmentation and the development of suitable messages.

Some of the key findings on attitudes to issues around illicit tobacco products and buying behaviours are given below:

- Smoking prevalence in the North of England is 23% overall with 14% of 14-15 yr olds and 29% of 16-17 yr olds;
- 1:5 smokers buys illicit product; this is more likely in hand rolled tobacco smokers with highest rates of purchase in the North East;
- More likely to be young male buyers and sellers but does span all social classes;
- A third of all smokers aged 14-17 buy illicit and on average this accounts for almost half of total consumption;
- Notable differences between rural and urban areas;
- On average; illicit buyers smoke two more cigarettes per day than non illicit smokers (18 v 16);
- Of illicit products purchased; 19% were a foreign brand with 25% felt to be counterfeit product;
- Buyers are motivated through price, convenience (bulk) and availability;
- Buyers are not put off by potential ‘undesirable’ substances

However

- 57% of population classified as “very uncomfortable” with the sale and purchase of illicit tobacco;
- 27% of population are likely to report if they suspect illicit product is being sold; rising to 75% if sales to children were suspected;
- Just under a third associate the illicit tobacco trade with forms of major crime;
- High agreement levels with statement “illicit tobacco trade is a danger to kids” (c80%);
- High agreement levels with statement “trade brings crime into the community” (c70%);
- 64% of buyers indicate that illicit product “makes it possible to smoke when they could not afford to otherwise”.



The economic cost of illicit tobacco products

The General Household Survey has provided the underlying data for the cigarette and Hand Rolling tobacco tax gap since 2001; a tax gap is the difference between the tax collected and that which HMRC believe should be collected.

Measuring tax gaps⁸

Cigarettes: Illicit market and associated revenue gaps*

| | 2003-04 | 2004-05 | 2005-06 | 2006-07 | 2007-08 |
|---|---------|---------|---------|---------|---------|
| Illicit Market Shares | | | | | |
| Upper Estimate | 21% | 19% | 19% | 18% | 15% |
| Mid-point of range | 18% | 15% | 15% | 14% | 10% |
| Lower Estimate | 15% | 11% | 10% | 10% | 4% |
| Associated Revenue Losses (£million) | | | | | |
| Upper Estimate | 3,000 | 2,600 | 2,500 | 2,300 | 1,900 |
| Lower Estimate | 1,900 | 1,400 | 1,200 | 1,100 | 500 |

The cigarettes revenue tax gap has shown a downward trend since 2003-4 largely because consumption has fallen faster than the receipt of excise duty.

HRT: Illicit market and associated revenue gaps*

| | 2003-04 | 2004-05 | 2005-06 | 2006-07 | 2007-08 |
|---|---------|---------|---------|---------|---------|
| Illicit Market Shares | | | | | |
| Upper Estimate | 60% | 64% | 63% | 59% | 52% |
| Mid-point of range | 53% | 59% | 57% | 53% | 47% |
| Lower Estimate | 45% | 54% | 52% | 47% | 41% |
| Associated Revenue Losses (£million) | | | | | |
| Upper Estimate | 840 | 980 | 940 | 900 | 750 |
| Lower Estimate | 520 | 700 | 650 | 610 | 500 |

* Includes duty and VAT. Figures are independently rounded to the nearest £100m of 1%

There is no clear trend in the hand rolled tobacco illicit market share.

Meeting our Challenges – Autumn Performance Report 2009 (HMRC)⁹ provides additional information.

The impact on health

All cigarettes are harmful to health

There is no evidence that smoking illicit (including counterfeit) tobacco is any more harmful to health than smoking legal duty-paid tobacco. It is imperative that a consistent message is given that illicit products are no more of a threat than their duty-paid counterparts, which will kill one in two of all life-long smokers.

The greatest threat posed is to the health of our most deprived communities, where there is often an inter-generation cycle of health inequalities caused by the poorest young people's early addiction to readily available cheap tobacco.

Research commissioned by ASH (Action Smoking and Health), found that one in four of the poorest smokers buys illicit tobacco product compared to one in eighth of the most affluent¹⁰.



National strategies to tackle the problem

In 2000, the government introduced a **Tackling Tobacco Strategy** which saw the reduction of smuggling into the UK. In 2001, a Fiscal Mark¹¹ was placed on all tobacco products packaging making it easier to identify if an item is duty paid or not. By 2006, the government had moved to a new phase and introduced **'New responses to new challenges: Reinforcing the Tackling Tobacco Smuggling Strategy'**¹².

This emphasised the new challenges that were emerging with regards to counterfeit tobacco and the increase in the smuggling of hand rolled tobacco. This meant that greater resources were required in order to monitor and strengthen the key points along the supply and distribution chain.

In 2008, the Government announced that the UK Border Agency and HMRC would work together on a new strategy – "Tackling Tobacco Smuggling Together. An integrated strategy for HM Revenue & Customs and the UK Border Agency"¹³. The UK Border Agency has responsibility for the detection and seizing of smuggled tobacco at UK border points and HMRC has responsibility for the detection and disruption of illicit supply inland.

A joint Department of Health and HMRC communications strategy is expected to be published in 2010; this will be available via the websites of both organisations.

Who are the main players in enforcement?

HM Revenue and Customs (HMRC)¹⁴ is the lead agency responsible for tackling the illicit trade in tobacco products. The operational responsibility for enforcement at UK borders is the responsibility of the UK Borders Agency (UKBA)¹⁵. Trading standards are the primary agency that enforce legislation regarding the sale of these products.

Council Trading Standards services have a key role to play at a local level detecting and seizing illicit tobacco products as appropriate. At regional level, joint operations with HMRC may be required to tackle the supply chain. In all cases, the sharing of intelligence between organisations is key to the success of the operation.

The LACORS and HMRC joint protocol¹⁶ on the lawful exchange of information establishes the mutually beneficial working practices between HMRC and Trading Standards in order to increase the effectiveness of activities taken to combat the supply of illicit tobacco products in the UK.

The protocol provides a framework for joint working and sharing information that will be of benefit to both in the delivery of their strategic objectives. Primarily the protocol delegates certain powers that are available to HMRC officers in respect of the seizure of tobacco products to Trading Standards in accordance with S14 Commissioners of Revenue and Customs Act 2005.¹⁷



Regional strategies

The development of multi-agency partnerships designed to tackle the supply of illicit tobacco products in a coordinated way is seen as the best way forward. Typically the partnerships include HMRC, Trading Standards, the police, the NHS, local tobacco alliances, local businesses and community leaders.

The North of England collaboration between the North East, North West and Yorkshire and Humber Regions, produced one of the first action plans developed specifically to tackle this problem. "Tackling illicit tobacco for better health"¹⁸ was launched in 2009 and sets out plans for the next three years.

The objectives of the programme are:

- Developing partnerships (between healthcare providers, trading standards, HMRC, police and local government)
- Engaging health and community workers (through training and sharing information)
- Generating and sharing intelligence (about illicit tobacco and associated crime)
- Identifying informal markets and preventive action (getting to the hot spots of the problem)
- Deliver enforcement (against regional priorities agreed with enforcement partners) agencies
- Marketing and communication (to raise the awareness if the public and other stakeholders)
- Working with business (raising employers awareness of the risks associated with illegal trading on their premises)
- Assessing progress (by tracking the performance of and benefits delivered by the programme)

The Legislation - HMRC

Trading Standards have delegated powers by virtue of S14(1) (c) of the Commissioners of Revenue & Customs Act 2005¹⁹ to seize or detain tobacco products in respect of a number of offences committed under HMRC legislation however, in most cases this is likely to be limited to the following:

S8G Tobacco Products Duty Act 1979 (TPDA)²⁰

Tobacco products, that is cigarettes and hand rolling tobacco that are required to bear a fiscal mark (whether counterfeit or not) and which do not, are liable to forfeiture.

Any person who is on possession of, transports or displays; or Sells, offers for sale or otherwise deals in unmarked tobacco products commits an offence.

The penalty is a fine up to a maximum of £5000.

S8J Tobacco Products Duty Act 1979

Products bearing fiscal marks which have been altered or overprinted are liable to forfeiture

It is important that Trading Standards establish contact with HMRC officers so that any seized goods can be passed over with minimal complication.



Other offences

Customs & Excise Management Act 1979 ²¹(CEMA)

Section 139 gives officers the power to seize goods that are liable to forfeiture under customs and excise acts. Section 7(2) of the TPDA provides that any goods in respect of which any person fails to comply with regulations made by the Commissioner, will be liable to forfeiture.

In the case of counterfeit tobacco that does not bear the fiscal make HMRC can seize the product on the basis that duty has not been paid at the time of manufacture or importation or at any subsequent duty point.

S170 Fraudulent evasion of excise duty (CEMA)

Where any person knowingly acquires possession of excise goods which excise duty has not been paid and does so with the intention of fraudulently evading payment of duty, are guilty of an offence.

The maximum penalty is a fine and imprisonment of up to 7 years.

This section is usually used in connection with those engaged in large scale smuggling to tobacco products.

S170a handling goods subject to unpaid excise duty (CEMA)

If after the excise duty point for any goods which are chargeable with a duty of excise, a person acquires possession of those goods or is concerned in carrying, removing, depositing, keeping or otherwise dealing them: and at the time when he acquires possession of those goods, the duty has not been paid, the conduct of that person attracts a penalty under S9 of the Finance Act which is calculated by reference to the amount of unpaid duty.

S170b Offence of taking preparatory steps for evasion of excise duty (CEMA)

If any person is knowingly concerned in the taking of steps with a view to the fraudulent evasion of excise duty, he is liable on summary conviction to a penalty or imprisonment for a term not exceeding 6 months or to both. If convicted on indictment, he is liable to a penalty of any amount or to imprisonment for a term not exceeding 7 years or both. Where any person is guilty of an offence under this section, the goods in respect of which the offence was committed are liable to forfeiture.

The Legislation – Trading Standards

Legislation enforced by Trading Standards does not permit HMRC officers to seize or detain goods; nor does the legislation provide any additional powers of search or entry to premises for HMRC officers.

Copyright, Design and Patents Act 1988²²

This Act establishes legal protection for designs and creates a criminal offence to combat counterfeiting. It also controls the making, importing or distributing of infringing copies of copyright material.

Trade Marks Act 1994²³

This Act exercise controls over the use of registered trade marks. Section 92 provides the powers for Trading Standards to detain or seize counterfeit or suspected counterfeit tobacco products.

Consumer Protection from Unfair Trading Regulations 2008²⁴

These Regulations prohibit traders/ businesses in ALL sectors from using unfair commercial practices towards consumers.



Use of tobacco readers

The reader is a hand-held device that can be easily transported to identify counterfeit and non-duty paid tobacco. All packs manufactured on or after 1st October 2007 by the four largest tobacco companies, which represent 97% of the UK duty paid market, have an anti-counterfeit mark incorporated into the pack. Hand-rolling tobacco packs are similarly marked since October 2008. The reader detects the mark and identifies if the product is genuine.

If a local council opts to purchase a reader, then any changes to the programming of the readers which may be required as a result of changes to the security feature, or other required upgrading, must be organised with the supplier of the readers and paid for directly by the local council. Until any such required update/upgrade is completed then the reader(s) must not be used.



The contact details of the supplier and conditions of sale are available from the Tobacco Manufacturers' Association on request. Contact 020 7544 0100.

The supplier of the readers will provide the Tobacco Manufacturers' Association and HMRC with the contact details of any purchasers in order to ensure that best practice and other relevant information can be shared. LACORS will also notify councils when an upgrade is required, when advised by Tobacco Manufacturers' Association and/or HMRC.

CASE STUDIES

CASE STUDY 1: Scambusters & HMRC join forces in the Midlands

Executive Summary

Additional funding of £80,000 has been used to employ two agency staff to build partnership arrangements with HMRC and the Police. The combined experiences and powers of the partnership members has led to some major seizures of tobacco products.

A major importer of products is currently being investigated with assets in excess of £1m. This in its own right will, through the use of Proceed of Crime Act, demonstrate the effectiveness of the additional funding and the strength of the partnership.

Nationally the Treasury loses approximately some £1.7bn each year in lost revenue through this type of activity.

Key Findings

To date nearly 1 million cigarettes and approximately 110 kg of H.R.T have been seized together with a number of vehicles and cash. A large number of operations were investigated using the expertise and powers of the major agencies. These were particularly relevant in the areas of surveillance. The building of the partnership was the foundation of the success of this project. It took some considerable time; around two months to establish, but the strength of the partnership has grown.

The value of the products and assets seized is around £250,000; this gives a return of around 3.1: 1 in terms of cost of project against the goods seized. This calculation does not take into consideration the disruptive effect of operations.

Given the OFT impact assessment on Trading Standards estimates that Consumer detriment, without intervention, would have continued for further two years and the officers have been fully functioning for ten months, a far higher figure can be attributed.

This type of activity is defined as a “lifestyle” activity under the Proceeds of Crime Act (POCA) and, as such, the assets of a suspect are vulnerable to forfeiture, an Accredited Financial Investigator has been seconded to the team to ensure that POCA is embedded into all such investigations from the outset.

A large number of interventions seized stock, estimates from officers have been gathered concerning the stock turnover were taken and included in the overall calculations.

The smaller retail values were estimated at one months supply, with larger stocks three months.

Overall, including the estimated value of disruption, equates to some £2m, giving a ratio of some 25:1. The Trading Standards average for Fair Trading work is around 6:1.

This should however be considered in the light that the partnership may have been tackling crime that to some extent had not been tackled previously in such a manner or approach. Nonetheless it represents very good value to the taxpayer.

Conclusions

The project demonstrated excellent value for money and the benefits of partnership working. The strength of the partnership lies in the different skills set, experiences and powers. It would be highly appropriate especially in today's economic climate, to seek to embed such a partnership into Trading Standards work.

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CASE STUDY 2 : Cannabis and counterfeits

In December 2008, thousands of pounds worth of cannabis and counterfeit tobacco products were seized and four people arrested as part of action taken by the Yorkshire and Humberside 'Scambusters' team. Operation APUS involved trading standards, HM Revenue & Customs and the police, targeting addresses across the region suspected of taking deliveries of significant quantities of counterfeit cigarettes and hand rolling tobacco. Officers uncovered a cannabis factory in Leeds, in which every room had been converted for cannabis production.

Approximately 500 plants were seized for destruction, the crop having an estimated street value in excess of £120,000. One person was arrested. A counterfeit cigarette factory was discovered in Leeds and another in Sheffield resulted in the seizure of over 58kilos of counterfeit tobacco and manufacturing paraphernalia. Two people arrested were suspected of being illegal immigrants. One person was been arrested and 10,000 counterfeit cigarettes were seized from an address in Hull. In addition a wealth of intelligence has been gained which will inform future operations against counterfeit tobacco.

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CASE STUDY 3 : Double duty

Working with HMRC officers, local police and the Scambusters team Trading Standards East Midlands officers have seized over half a million non duty paid cigarettes since the beginning of 2009 and a significant quantity of hand rolling tobacco.

Using his initiative on an underage test-purchasing exercise an officer took a volunteer to target premises and managed to get two underage sales of non-duty paid cigarettes. Using the specialist surveillance skills of the regional Scambusters team to identify premises and owners, work is now being undertaken with Immigration Officers to check the status of sellers.

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CASE STUDY 4 : Illicit tobacco in Barnsley

Following reports that a local Tanning Studio was selling illicit cigarettes, Barnsley Trading Standards Service seized 2000 cigarettes from a business in the city.

Further enquiries by the Service revealed that the trader had been operating a lucrative sideline in selling illicit tobacco and uncovered evidence which showed that, over an 8 month period, the trader had sold 50,000 illicit cigarettes from the premises of the Tanning Studio. Enquiries are continuing into this trader.

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CASE STUDY 5 : North of England Trading Standards & HMRC join forces

There has been considerable joint working with HMRC Inland Detection Teams at a range of premises, including an indoor market, domestic property and small businesses, in the biggest seizure 6500 counterfeit cigarettes were taken by HMRC and handed to Trading Standards for further action, other items seized have included fireworks and counterfeit clothing.

These activities have produced a considerable amount of intelligence relating to the cheap and illicit market and officers have found examples of smuggled cigarettes, counterfeit cigarettes and 'cheap whites' notably Jin Ling. In a recent Police operation over 14,000 Jin Ling were seized from a house, identified by a Trading Standards enforcement officer and signposted to HMRC for their action.

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CASE STUDY 6 : Four arrested in regional day of action

On 16th September 2009, four people were arrested (three of whom were suspected to be illegal immigrants) for being in possession of suspected counterfeit cigarettes and hand rolling tobacco. The arrests were made as part of a regional day of action, code-named Operation APUS 2, which involved trading standards officers from West Yorkshire, Rotherham and Barnsley, the regional Scambusters Team and HMRC. The results of the operation, which involved the simultaneous execution of search warrants across the region, included:

- Four people arrested for being in possession of suspected counterfeit cigarettes and hand rolling tobacco;
- 25,000 counterfeit cigarettes were seized;
- 80 Kg of illicit leaf tobacco was seized;
- A quantity of boxes of non UK duty paid cigarettes which were linked to a smuggled shipment of 21 million cigarettes

One of the addresses searched, was a "fag house" where illicit cigarettes were found stashed under the bed and Jin Ling cigarettes were stored in a wardrobe. A cash drawer was also found in the living room for gathering the takings. During the search, five separate individuals knocked on the door, asking to buy cigarettes which indicates the extent of the operation. Further evidence was uncovered that single cigarettes were being sold to children from the property

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CASE STUDY 7 : Chinese whispers?

Chinese students in the North West Region were importing illicit cigarettes into the UK through postal packages from their homeland. Trading Standards North West (TSNW) learnt that there was a lack of understanding among the educational establishments and the students themselves about the illegality of the trade. A pilot project with the University of Central Lancashire was established using Freshers week as an opportunity to inform students of the illegality of their actions.

4000 postcards and Cartoon strip leaflets in English and Chinese were produced for the student induction packs sent out just prior to Freshers week. The message focused around the fact that dealing in illicit cigarettes is illegal and the easy money earned could lead to an unlimited fine, long jail sentences and a criminal record – “say no to illegal cigarettes and yes to your career”.

The information was also turned into posters to be displayed from the beginning of October in Halls of Residence and the

Students Union. UCLAN also agreed to display slogans on plasma screens and as screensavers on university computers.

10,000 fortune cookies were also produced each resembling a normal fortune cookie but when broken, the slogan did not say “you will meet a tall, dark, handsome stranger” but rather “if you sell illegal tobacco you are killing four times as many people as if you sell illegal drugs” and “through buying and selling illicit tobacco you are funding organised crime”.

All of the material includes both the Consumer Direct and Crimestoppers numbers for reporting of suspicious activity, which will enable TSNW to evaluate the effectiveness of the campaign.

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