

All Party Parliamentary Group on Smoking and Health Inquiry into the Illicit Trade in Tobacco Products

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Introduction

1. The tobacco industry claims that “plain” (standardised) packaging of cigarettes and other tobacco products would increase the level of illicit tobacco in the UK market.
2. For example, the British American Tobacco website includes the following statement: *“We believe a policy designed to make tobacco less accessible to youth could actually end up having the opposite effect — by increasing the black market and making the products cheaper and more accessible. Generic packaging would make it harder to prevent smuggled and counterfeit products entering a market, eroding government tax revenue and disrupting efforts to tackle the illegal trade in tobacco products that plays a significant role in funding international crime and terrorism.”*¹
3. This memorandum suggests that there is no good evidence for the industry’s claims. It also looks at the historic role of the tobacco industry in smuggling, the changing nature of the illicit tobacco trade in the UK, health concerns relating to illicit cigarettes, and the key causes of the illicit tobacco trade.

Illicit Trade: Industry Involvement

4. Recent tobacco industry concern about illicit trade might be considered ironic, since major manufacturers have a long history of involvement in smuggling operations. Since 2004, the four major international tobacco companies have paid billions of dollars in fines and payments to settle cigarette smuggling litigation in Europe and Canada.
5. Evidence of the direct and indirect involvement of the tobacco industry in this large scale fraud is well documented, through the industry’s internal documents,² their own admissions³ and court judgements.⁴ In 2000 the

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http://www.bat.com/group/sites/uk_3mnfen.nsf/vwPagesWebLive/DO7J7DCZ?opendocument&SKN=1

accessed 12 October 2012.

² Collin J, LeGresley E, MacKenzie R, Lawrence S, Lee K. Complicity in Contraband: British American Tobacco and Cigarette Smuggling in Asia. *Tobacco Control* 2004;13 (Supplement II):ii96-ii111. Lee K, Collin J. 'Key to the future': British American Tobacco and cigarette smuggling in China. *PLoS Medicine* 2006;3 (7):228-37. LeGresley E, Lee K, Muggli M, Patel P, Collin J, Hurt R. British American Tobacco and the "insidious impact of illicit trade" in cigarettes across Africa. *Tobacco Control* 2008;doi:10.1136/tc.2008.025999

³ Clarke K. Dilemma of a cigarette exporter. *Guardian*, 3 February 2000.

deputy chairman of BAT stated that: *"Where any Government is unwilling to act or their efforts are unsuccessful, we act, completely within the law, on the basis that our brands will be available alongside those of our competitors in the smuggled as well as the legitimate market."* In July 2008 and April 2010 in Canada, three tobacco companies pleaded guilty and admitted "aiding persons to sell or be in possession of tobacco products manufactured in Canada that were not packaged and were not stamped in conformity with the Excise Act", while Northern Brands International Inc., a company related to RJR, pleaded guilty to a conspiracy offence under the Criminal Code.⁵

6. Currently, a major tobacco company, JTI, is under investigation by the European Union's Anti-Fraud Office OLAF for alleged involvement in smuggling operations in the Middle East.⁶

Tobacco Smuggling in the UK: Previous History

7. Tobacco smuggling was recognised as a serious problem in the UK in the 1990s. British Customs and Excise (Customs) estimated that the illicit cigarette market increased from 3% of total UK consumption in 1996-97 to 21% in 2000-01. In 2000-01 and 2001-02 it totalled about 16 billion cigarettes, and seizure evidence suggests that as many as half of them were smuggled *Regal* and *Superkings*, an Imperial Tobacco brand.⁷
8. These two brands were exported in huge quantities to places where the intended market was 'unclear', then were illegally imported through smuggling networks back into the UK. Customs believe that in 2000-01 up to two thirds of the 12 billion *Regal* and *Superkings* exported by Imperial were smuggled illegally back into the UK. From October 2000 to September 2002 a third of all *Regal* and *Superkings* were exported to Moldova, Latvia, Russia (including Kaliningrad), Afghanistan and Andorra.⁸
9. In May and June 2002 the UK Parliament's Public Accounts Committee held hearings on illicit trade. . George Osborne MP, then a member of the Committee, memorably made the following point to the Chief Executive of Imperial Tobacco: *"one comes to the conclusion that you are either crooks or you are stupid, and you do not look very stupid. How can you possibly have sold cigarettes to Latvia, Kaliningrad, Afghanistan and Moldova in the expectation that those were just going to be used by the indigenous population*

⁴ Canada Revenue Agency. "Federal and provincial governments reach landmark settlement with tobacco companies". Québec, Canada Revenue Agency, Press release, July 31 2008, <http://www.cra-arc.gc.ca/nwsrm/rlss/2008/m07/nr080731-eng.html>, accessed October 2012.

⁵ Canada Revenue Agency. "Federal, provincial, and territorial governments conclude landmark settlements with tobacco companies" Press Release. 13 April 2010. <http://www.cra-arc.gc.ca/nwsrm/rlss/2010/m04/nr100413-eng.html>. Accessed October 2012

⁶ Solomon J, EU probes cigarette deal that may have aided Syria, The Wall Street Journal, August 21, 2012. <http://online.wsj.com/article/SB10000872396390444233104577595221203321922.html>

⁷ House of Commons, Committee of Public Accounts. Third report: tobacco smuggling, HC143. London, Houses of Parliament, 2003.

<http://www.publications.parliament.uk/pa/cm200203/cmselect/cmpubacc/143/14302.htm>, accessed October 2012. Full transcript (16):

<http://www.publications.parliament.uk/pa/cm200203/cmselect/cmpubacc/143/2061901.htm>

⁸ *ibid*

or exported legitimately to neighbouring countries, and not in the expectation they would be smuggled? You must know - you only have to read a newspaper every day, a member of the public could tell you - these are places which are linked to organised crime, that the drugs trade passes through all of these countries, that prostitution passes through all these countries. Did you not know that?"

10. Since these hearings in May 2002 exports of *Superkings* and *Regals* to suspected markets have been greatly reduced. The illicit cigarette market in the UK dropped from 20% of overall consumption in 2001-02 to 16% By 2006-7, *Regal* and *Superkings* seizures, had fallen to fewer than 5 million cigarettes, just 1% of seizures of genuine UK brands.⁹
11. In 2000, the UK Government announced an anti-smuggling Action Plan, which included scanners for container detection, prominent fiscal marks on packs, increased punishment, confiscation of offenders' assets, more customs officers, and a campaign to increase public awareness.¹⁰ The Plan has been regularly updated since, and an effective partnership has been created between HM Revenue and Customs (HMRC) and the UK Border Agency (UKBA).
12. The UK Finance Act 2006 placed a legal duty on tobacco manufacturers not to facilitate smuggling, and manufacturers who fail to take sufficient steps to prevent their products being smuggled into the UK face fines of up to £5 million¹¹.

The Changing Nature of Illicit Trade

13. When large scale smuggling of genuine cigarette brands to the UK decreased, the proportion of counterfeit cigarettes, hand-rolling tobacco, and 'illicit whites' increased.¹² 'Illicit whites' are cigarettes produced often quite openly and at known locations, mostly outside the European Union, but are primarily intended for the illegal market of another country. As manufacturing is apparently in accordance with national legislation and is either not or at best minimally subject to national controls, the manufacturers can buy sophisticated machinery without risk of confiscation. Under these conditions a reasonable standard of quality in the production process can be achieved.
14. The best known illicit white brand in the UK and the rest of Europe is Jin Ling, a cigarette brand with a Chinese name, manufactured in Russia, in appearance in accordance with Russian domestic law, with the look and the taste of an American blend (Camel), but destined for the illegal market in the EU. Jin Ling rapidly became one of the most seized cigarette brands in the

⁹ HM Revenue & Customs. Departmental Autumn Performance report 2007. London, HM Treasury, 2007

¹⁰ HM Customs & Excise. Tackling Tobacco Smuggling. London, HM Treasury, 2000

¹¹ HM Revenue & Customs. £5m penalties for tobacco manufacturers who aid smuggling, press release. London, HM Revenue & Customs, 29 September 2006

¹² HM Revenue & Customs, Tackling Tobacco Smuggling – building on our success. A renewed strategy for HM Revenue & Customs and the UK Border Agency. April 2011

EU.¹³ Jin Ling is produced in the Free Zone of Kaliningrad and profits from the Free Zone regime, which generally is characterised by relief from Customs duties, formalities and procedures.¹⁴ In 2009/10, illicit whites accounted for 46% of large scale cigarette seizures in the UK.¹⁵

Are Illicit Cigarettes More Dangerous to Health?

15. Counterfeit cigarettes are illegally manufactured and are often described, by Government agencies including HMRC and police, as more dangerous than legally produced cigarettes. For example, according to a 2004 Customs and Excise report, counterfeit cigarettes produced in China contain higher levels of tar, nicotine, carbon monoxide and cadmium than lawfully sold cigarettes.¹⁶
16. Counterfeit cigarettes are not a standard and uniform product.. Some counterfeits are made of good quality tobacco and some may include musty raw tobacco processed with sulphur and carbamide to look better.¹⁷
17. While the content of some counterfeit cigarettes raises concern, the way smokers inhale and smoke counterfeit cigarettes is not known. Customs research in the UK showed that 78% of smokers said the counterfeit cigarettes did not taste the same as genuine ones, and 25% said the cigarette themselves fell apart more quickly. Smokers reported that *“they smell different, they taste different, they’re too harsh and they don’t draw easily”*.¹⁸ Several young smokers in focus groups in Scotland reported becoming ill after smoking counterfeit cigarettes, with mention of colds, chest infections and sore throats. *“You get a cold or you get ill after smoking four or five.”* (Male, 18–24 years, C2DE)¹⁹
18. All these factors might influence the smoking behavior of counterfeit users, for example they may inhale less deeply or smoke fewer cigarettes. The health damage to smokers is not only determined by the content of the cigarettes, but by the way they are smoked.
19. In addition, highlighting the dangers of counterfeit cigarettes may risk communicating an unintended message that genuine cigarettes are normal and safe. BAT in Nigeria for instance notoriously claimed that: *“tobacco use is*

¹³ Shleynov R, Candea S, Campbell D, Lavrov D. Made To Be Smuggled. Russian contraband cigarettes ‘flooding’ EU. The Center for Public Integrity: Washington, 2008

¹⁴ Customs Co-operation Council (World Customs Organization), International Convention on the Simplification and Harmonization of Customs Procedures, (as amended), Revised Kyoto Convention, WCO, Brussels, 1999.

¹⁵ HM Revenue & Customs, Tackling Tobacco Smuggling – building on our success. A renewed strategy for HM Revenue & Customs and the UK Border Agency. April 2011.

¹⁶ HM Customs & Excise, Counterfeit cigarettes 2004, HMCE, 2004.

¹⁷ Shen A, Antonopoulos GA, Von Lampe K. ‘The Dragon Breathes Smoke’: Cigarette Counterfeiting in the People’s Republic of China. British Journal of Criminology 2010; 50:239-258.

¹⁸ HM Customs & Excise, Counterfeit cigarettes 2004, HMCE, 2004.

¹⁹ Moodie C, Hastings G, Joossens L. Young adult smokers’ perceptions of illicit tobacco and the possible impact of plain packaging on illicit tobacco purchasing behaviour, European Journal of Public Health, Advance Access, 26 March 2011

risky, but counterfeit cigarettes are lethal".²⁰ Scientists have identified about 4,000 different chemicals in tobacco smoke of "regular" cigarettes. Focusing on the hazardous chemicals in counterfeit cigarettes may mean that "regular" cigarettes are seen as safer, while in fact they contain 70 carcinogenic chemicals²¹ and are responsible for 6 million premature deaths each year. Both genuine and counterfeit cigarette are extremely toxic products. There are no safe cigarettes and there is no safe level of smoking and it is important that no official communications in relation to smoking undermine this key message.

20. The primary health concern in relation to illicit cigarettes should be not their toxicity, but their lower price, which may lead to increased tobacco use. If the illicit tobacco trade were eliminated, there would be an overall increase in tobacco prices and a consequent fall in consumption and tobacco related deaths. In 2008, Robert West and colleagues calculated for the UK that without tobacco smuggling about 4000 premature deaths a year could have been prevented.²²

Will Plain Packaging Lead to More Smuggling?

21. The tobacco industry is strongly opposed to "plain" (more accurately "standardised") packaging. One of the main arguments is that the introduction of plain packaging will lead to more smuggling. For example, on 9 March 2011, Christopher Ogden, then Chief Executive of the Tobacco Manufacturers' Association (TMA), commented: *"The TMA is strongly opposed to the principle of plain packaging (...) Plain packs are also likely to lead to yet further increases in the smuggling of tobacco products and plain packs would make it so much easier for a counterfeiter to copy than existing branded packs making it even more difficult for a consumer to differentiate between genuine and counterfeit products."*²³
22. This argument is in my opinion very weak. For example it depends on misleading representations of a plain pack, on poor evidence, and on wrong assumptions.
23. **Misleading representation of a plain pack:** In general, the tobacco industry describes a plain pack as a white or one color pack with a text warning. All packs would look the same and would be easy to copy. In fact, plain cigarette packets will always have large pictorial health warnings and such packs will therefore be as difficult to counterfeit as any other pack.
24. **Wrong assumptions:** The tobacco industry claims that plain packs would be easier to counterfeit. But in fact they know that all packs, including those with

²⁰ Cover Tobacco Control April 2005, vol14, nr2

<http://tobaccocontrol.bmj.com/content/12/3/250.extract/reply#content-block>

²¹ IARC Monographs on the Evaluation of Carcinogenic Risks to Humans. Volume 100E (2012) A review of human carcinogens: personal habits and indoor combustions.

²² West R, Townsend J, Joossens L, Arnott D, Lewis S. Why combating tobacco smuggling is a priority. BMJ 2008;337:1028-1029 (1 November 2008).

²³ TMA, [TMA responds to Government's Tobacco Control Plan](http://www.the-tma.org.uk/2011/03/tma-responds-to-governments-tobacco-control-plan/), 9 March 2011, accessed October 2012

tax stamps, are easy to counterfeit. A cover story in Business Week in 2005 described the counterfeit trade: *“Counterfeiters are now so proficient that forensic experts are sometimes needed to spot bogus products”*.²⁴ Counterfeiters are generally able to provide top quality packaging at low prices in a short time. The quality of counterfeit cigarette packs has substantially improved from the 1990s, making it difficult to distinguish counterfeit from genuine cigarette packs. In 2004, research from Customs and Excise showed that the outside pack was the least likely indicator of the carton being counterfeit.²⁵ Even tax stamps with more sophisticated security features are easy to counterfeit.

25. In 2010, the four major transnational tobacco companies signed an agreement to promote Codentify, a system that produces a visible and unique code printed onto tobacco packaging to identify each package, as a technological solution for track and trace and digital tax verification (intended inter alia to meet the requirements of Article 8 of the Illicit Trade Protocol). Mark Hill of Imperial Tobacco said that tax stamps are outdated, because they are easy to falsify: *“the overt security features on the stamps are easily and successfully copied by counterfeiters within a matter of weeks – in a quality to fool most consumers.”*²⁶ In a 2012 brochure on Codentify, Philip Morris International (PMI) confirms that packaging is easy to counterfeit: *“Paper-based tax stamps and fiscal markers are easily counterfeited, despite the inclusion of innovative holograms, special inks and elaborate design details. Evidence shows that counterfeiters can make copies of even the most sophisticated paper stamps in three weeks.”*²⁷
26. It is therefore fair to conclude that the tobacco industry is very inconsistent in its statements on counterfeiting. On the one hand they claim that plain packs are easy to counterfeit, on the other they insist that counterfeiters already copy all paper-based material at short notice, even the most sophisticated tax stamps.

Key Drivers of Illicit Trade

27. There is extensive evidence to show that other factors than packaging are the main drivers of illicit trade. Results from focus groups among young adults in Glasgow in 2010 showed that the participants would not change their illicit tobacco purchasing behaviour if cigarettes were sold in identically colored plain packs. The demand for illicit tobacco was related to price and availability, but not to packaging.²⁸ Research in the North of England concluded that buyers are significantly motivated to purchase illicit tobacco

²⁴ Balfour F, The global counterfeit business is out of control, Cover Story, Business Week, February 7, 2005, 44-51.

²⁵ HM Customs & Excise, Counterfeit cigarettes 2004, HMCE, 2004.

²⁶ Hill M, Digital Tax Verification (DTV) Codentify, The industry Standard, October 2010.

²⁷ Philip Morris International, Codentify, Brochure, 2012.

http://www.pmi.com/eng/documents/Codentify_E_Brochure_English.pdf

²⁸ Moodie C, Hastings G, Joossens L. Young adult smokers' perceptions of illicit tobacco and the possible impact of plain packaging on illicit tobacco purchasing behaviour, European Journal of Public Health, Advance Access, 26 March 2011

28. However, while the demand for illicit tobacco products is strongly influenced by price, the attractiveness of illicit trade to suppliers is more complex. Although a high tax margin may provide the initial incentive to smuggle, the data show clearly that it is not the only factor. Other important factors include the ease and cost of operating in a country, industry participation, how well organized crime networks are, the likelihood of being caught, the punishment if caught, corruption levels, and so on.³⁰
29. Illicit trade is a product of demand and supply: demand by smokers for cheaper or specific tobacco products which are not available on the domestic market, and supply by both legal and illegal tobacco manufacturers looking for more profit, more sales, increasing market shares or to penetrate new markets. Supply is facilitated by corruption, the presence of criminal networks and weak Government enforcement capacity.³¹ As the UK experience shows quite clearly, where these supply issues are addressed by law enforcement and Government agencies, the prevalence of illicit trade drops, even in markets with high tax levels. This policy was successful, as the illicit UK cigarette market was reduced from 21% in 2000-01 to 9% in 2010-11.³²
30. Supplying the illicit market is attractive to companies and traders because of the low cost of manufacturing, as low as 5 US cents a pack in Paraguay,³³ 20 US cents for a Jin Ling pack in Kaliningrad³⁴ or 20 US cents for a Chinese counterfeit pack.³⁵ PMI acknowledges that production costs are low and estimates the cost for a Chinese counterfeit pack at 15 pence.³⁶
31. The low manufacturing cost has two major consequences: the potential profits for selling illicit tobacco are very high and the potential savings from reducing the costs of manufacturing illicit cigarettes are very low.
32. Evading tax by diverting tobacco products into the illicit market generates a considerable profit margin for illicit traders. Organised smugglers can buy a

²⁹ NEMS, North of England Illicit Tobacco Survey, Billingham, 2009

³⁰ Joossens L, Merriman D, Yurekli A, Chaloupka F. Issues in the smuggling of tobacco products. In Jha P, Chaloupka F (Eds). Tobacco Control Policies in Developing Countries. Oxford, Oxford University Press, 2000.

³¹ Joossens L, Raw M, From cigarette smuggling to illicit tobacco trade, Tobacco Control 2012; 21:230-4.

³² HM Revenue & Customs, Measuring tax gaps 2012, October 2011. <http://www.hmrc.gov.uk/stats/measuring-tax-gaps.htm>

³³ Ramos A. The illegal trade in tobacco in the Mercosur Countries. Trends in Organised Crime 2009;12:267-306.

³⁴ Shleynov R, Candea S, Campbell D, Lavrov D. Made To Be Smuggled. Russian contraband cigarettes 'flooding' EU. The Center for Public Integrity: Washington, 2008

³⁵ Te-Ping Chen, China's Marlboro country, OCCRP, 2008, https://reportingproject.net/underground/index.php?option=com_content&view=article&id=9:chinas-marlboro-country&catid=3:stories&Itemid=22

³⁶ Philip Morris International. Standardised tobacco packaging will harm public health and cost UK taxpayers billions: A response to the Department of Health consultation on standardised packaging of tobacco products, 2012.

container of Jin Ling cigarettes in Russia (on which they pay no taxes) for US\$100,000. The value of such a container in the EU is on average US\$2 million, an enormous profit margin.³⁷ In the UK the potential profit is as much as three times higher.

33. Since manufacturing costs for illicit cigarettes are so low, reducing them further would be difficult. Research commissioned by PMI has claimed that plain packaging without the different features of the brand (e.g. logo's, relief drawings, images or other embellishments) would significantly cut production costs.³⁸ However, this is not a credible assumption. If the production cost of a counterfeit pack is 10 to 15 pence, the packaging cost can reasonably be estimated at about 2 to 6 pence and possible savings to those costs from plain packaging at no more than 1 to 3 pence.
34. The industry has also argued that plain packaging will lead to more price competition among unbranded packs, lower prices and increased consumption.³⁹ A price war following the introduction of plain packaging cannot be entirely excluded as a possibility, since it is the responsibility of the tobacco companies to set prices. If tobacco companies want to launch a price war, nobody can prevent them. Governments cannot at present regulate prices (although setting minimum prices is certainly a policy option for the future), but they can increase taxes to annul the effect of the price reduction. This will not lead to an increase of smuggling if tax enforcement and tax administration is strengthened.

Tax and Smuggling

35. The tobacco industry and its lobbyists routinely claim that high tax levels lead inevitably to high levels of illicit trade. But for the reasons stated in paragraph 28, the true picture is much more complex. In fact, smuggling is more common in low tax countries than in high tax countries.
36. Estimates of illicit trade in 84 countries in 2007 showed that the proportion of the cigarette market is overall lower in high income countries than in low income countries.⁴⁰ Corruption has been shown to be a strong predictor of levels of tobacco smuggling, with inadequate laws and law enforcement as well as geography also playing a role.⁴¹

³⁷ Shleyonov R, Candea S, Campbell D, Lavrov D. Made To Be Smuggled. Russian contraband cigarettes 'flooding' EU. The Center for Public Integrity: Washington, 2008

³⁸ Transcrime. Plain packaging and illicit trade in the UK: Study on the risks of illicit trade in tobacco products as unintended consequences of the introduction of plain packaging in the UK. Milan: Transcrime: Joint Research Centre on Transnational Crime, 2012.

³⁹ Philip Morris International. Standardised tobacco packaging will harm public health and cost UK taxpayers billions: A response to the Department of Health consultation on standardised packaging of tobacco products, 2012.

⁴⁰ Joossens L, Merriman D, Ross H, Raw M. The impact of eliminating the global illicit cigarette trade. *Addiction* 2010;105:1640-9.

⁴¹ Merriman D, Yurekli A and Chaloupka F. How big is the worldwide cigarette-smuggling problem? In: Jha P and Chaloupka F., eds. *Tobacco Control in Developing Countries*. 2000

37. Recent research on illicit tobacco in 18 European countries, conducted in 2010 through the Pricing Policies and Control of Tobacco in Europe (PPACTE) project, also showed that illicit tobacco trade had no significant association with the cigarette price. Smokers from countries where a 20-cigarette pack of Marlboro costs less than €3 were more frequently cigarette tax evaders. The data also showed that illicit trade is more frequent in European countries with a land or sea border with Ukraine, Russia, Moldova or Belarus, which are major suppliers of cheap and illicit cigarettes.⁴² The findings are in line with a European Commission report showing that these four former Soviet countries are major sources of illicit cigarettes and alcohol in the European Union.⁴³
38. Price levels in any specific national market therefore do not in any simple way predict levels of illicit trade.

Conclusions

39. Effective action against illicit trade is entirely possible in countries with high tobacco tax levels, as the UK experience shows. Illicit trade is also highly unlikely to be seriously affected by the introduction of plain packaging legislation in the UK. The most effective way to reduce illicit trade is through effective Government and public agency co-operation, internationally, in Europe, at national, regional and local level. International agreement on the Illicit Trade Protocol, and the strong record of work on the issue by UK agencies together mean that levels of illicit trade can and should be further reduced, and that the introduction of plain packaging should not be blocked because of fears that illicit trade may rise.
40. Co-operation between law enforcement, customs agencies, trading standards and health services and health organisations is also important, to ensure that effective messages reach consumers who might be tempted to buy and consume illicit product.
41. The tobacco industry claims that plain packs are easier to copy and will lead to an increase in the level of tobacco smuggling. The track record of the tobacco industry, the make-up of the illicit market today, the evidence that all existing packs are easy to forge and the real causes of the illicit tobacco market show why the tobacco industry's claims make no sense.
42. In short, fighting illicit trade does not mean listening to special pleading from the tobacco industry. Instead, it requires "joined up" Government.

⁴² Joossens L, Lugo A, La Vecchia C, Gilmore A, Clancy L, Gallus S, Illicit cigarettes and hand rolled tobacco in 18 European countries: a cross-sectional survey. *Tobacco control*, 2012, in press.

⁴³ European Commission. *Action Plan to fight smuggling of cigarettes and alcohol along EU Eastern border*, SEC (2001), Brussels, 24 June 2011. http://ec.europa.eu/anti_fraud/documents/Working-paper.pdf