



## **Review of the supply of tobacco products in Jersey**

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## **Executive summary**

### ***Introduction to the market study***

The Minister for Economic Development requested the Jersey Competition Regulatory Authority (**JCRA**) to undertake a market study into the supply of cigarettes and hand-rolling tobacco in Jersey.

The request was prompted by concerns that the pre-tax prices of tobacco products (i.e. when VAT/GST and impôts/duties are removed) are significantly higher in Jersey than in the United Kingdom<sup>1</sup>. Concerns had also been raised regarding alleged profiteering by parties involved in the supply of tobacco products in Jersey; for example, retail prices increased markedly in January 2013 to reflect a substantial rise in impôts on tobacco on 1 January that year, but because of the time lag between the date of import and the date of sale, tobacco on which the higher duty rate had been levied would not have reached the shops until much later.

### ***Terms of reference***

The terms of reference for the market study asked the JCRA to:

1. review the level of pricing, costs and profit from the supply of tobacco products in Jersey at the wholesale and retail level; and
2. report on the extent of competition at each level of the supply chain and to consider whether steps could be taken to enhance competition or otherwise improve the operation of the market.

### ***Regulation of tobacco, and the aim of market studies***

For sound public policy reasons, the supply of tobacco is highly regulated. Smoking has serious health effects, and for that reason, packaging of tobacco supplied in Jersey is required to carry specific health warnings in English, which follow those used in much of the European Union (**EU**). In addition, duties on tobacco are high in most jurisdictions around the world, and rates have typically increased substantially in recent years. In Jersey, this has occurred as part of a strategy on the part of the States of Jersey to encourage people to stop smoking.

The JCRA recognises in the particular case of tobacco that there is an inherent tension between the aims of market studies (which are intended to report on the state of competition in a market and identify means of increasing competition, or delivering better outcomes for consumers, such as lower prices) and the explicit policy of the States of Jersey, which is to discourage smoking. All other things being equal, it would be expected that higher prices would lead to lower consumption. On this view, the fact that pre-tax prices for tobacco products are higher in Jersey than in the UK might be seen to be aligned with the policy direction of the States of Jersey.

However, as the data analysis in this report shows, by far the largest influence on the price of tobacco products in Jersey, Guernsey and the UK (and well as most other jurisdictions) is the rate of impôts/duties. This variable is directly controllable by the States of Jersey in pursuit of its policy objectives. In the JCRA's view, the fact that the existing market structure might produce higher prices than would otherwise be expected in a more competitive market structure is not a sound basis for failing to consider whether the market could operate more effectively. Moreover, the JCRA

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<sup>1</sup> As reported in the Retail Prices Comparison published annually by the States of Jersey Statistics Unit

is cognisant that this market study was requested by the Minister for Economic Development in light of the concerns outlined above.

This report therefore sets out various remedies that could be considered in order to improve competition for tobacco products. It will then be for elected officials to take account of the competing public policy considerations in deciding what further steps to undertake in pursuit of more effective competition.

### ***Features of markets for tobacco products in Jersey***

The markets for tobacco products in Jersey have a number of distinctive features:

- **Two importers with exclusive supply agreements with manufacturers:** The vast majority of tobacco products sold in the duty-paid market are imported by two companies: JJ Fox Trading Limited and Longueville Distributors Limited (a subsidiary of the Liberation Group). Both of these companies have exclusive agreements with manufacturers who supply to them, so no other companies can import these products to the Channel Islands. By contrast, in the UK, large retailers will typically deal directly with tobacco product manufacturers, rather than third-party distributors.
- **Channel Islands unique packaging:** The combination of highly-prescriptive packaging regulations and a desire on the part of customs offices in Jersey and elsewhere to prevent smuggling and ensure that tobacco duties are paid mean that the packets used for tobacco products sold in the duty-paid market in the Channel Islands are unique to the Channel Islands. We are told by the manufacturers and Channel Islands importers of tobacco products that that as a result, the production runs for cigarettes manufactured for the duty-paid market in the Channel Islands are very small.
- **Parallel importing is impossible:** The combination of packaging legislation and duty rules in the UK also means that parallel imports of tobacco products from the UK is presently impossible – it is illegal under UK law for cigarettes and hand-rolling tobacco with packaging carrying UK duty markings (i.e. “UK Duty Paid”) to be sold outside the UK.
- **High proportion of tobacco purchased duty-free:** Due to the geographic proximity of Jersey to other customs territories (e.g. France, Guernsey and the UK), and the very high propensity for Jersey residents to travel off-island on a regular basis, it is comparatively straightforward for Jersey residents to purchase duty-free tobacco products. In addition, the price difference between duty-paid and duty-free tobacco products is substantial, and growing (due mostly to increases in the rate of duties/impôts). As such, it is estimated that between 40 and 50% of the cigarettes smoked in Jersey are purchased duty-free, which is a considerably higher figure than in the UK.

### ***Comparisons of pre-tax prices for tobacco products in Jersey, Guernsey and the UK***

We collected price and cost data from various parties involved in the supply chain for tobacco products in Jersey, Guernsey and the UK, as well as duty free sales by premises in Jersey or air or sea carriers serving Jersey. Data for Jersey, Guernsey and the UK was available for seven of the top ten cigarette brands, and two of the top rolling tobacco brands, sold in Jersey.

Analysis of that data shows that net of tax and duty, cigarettes in the duty-paid market in Jersey are on average 89p per pack (or 55%) more expensive than in the UK, and 7p per pack more expensive than in Guernsey.

The contributors to that higher pre-tax price are across the supply chain: higher prices charged by manufacturers add 27p per pack, while differences in the gross margin attributable to import and retail activities add 62p per pack, relative to the UK. On its face, it is difficult to understand why the price difference would be so high. Cigarettes are easy to transport, since they are very light relative to their value. While they deteriorate over time, their maximum shelf-life is in the region of 6-12 months, rather than days or weeks. It should be noted that other estimates of the difference between the UK and Jersey in pre-tax prices for packs of 20 cigarettes – by the States Statistics Unit and one of the importers - show a smaller difference than is reported here.

We estimate that approximately 3.9 million packs of cigarettes are sold annually in the duty-paid market in Jersey<sup>2</sup>. Our analysis of price differences therefore suggests that consumers in Jersey pay approximately £3.4 million more annually for cigarettes in the duty-paid market than they would if cigarettes were priced on a pre-tax basis at the same level as in the duty-paid market in the United Kingdom.

Intriguingly, the patterns of pre-tax prices appear to be quite different for hand-rolling tobacco, which accounts for a much smaller portion of sales of tobacco products than cigarettes. To avoid disclosing confidential and commercially sensitive information we are prevented from disclosing our analysis of prices across the supply chain for hand-rolling tobacco. Nevertheless, the fact that trends in pre-tax prices are different for a product that is so similar to cigarettes provides us with further evidence that the market/s for the supply of tobacco products in Jersey may not be functioning optimally.

### ***Barriers to competition***

We have considered whether there are means of enhancing competition or otherwise improving the operation of the market/s for duty-paid tobacco products in Jersey. Our supposition is that the retail level of the supply chain has the potential to operate competitively – there are a significant number of competing retailers supplying tobacco products in Jersey, typically at supermarkets, convenience stores and fuel forecourts. Our focus has therefore been on whether the competition inherent at this level of the supply chain can be harnessed.

We have also considered whether there are means by which the existing geographic division of the supply of tobacco products – in which products supplied in the duty-paid market in the Channel Islands are specific to the Channel Islands - can be overcome. Tobacco products are almost the only example of goods in respect of which Jersey customers cannot access parallel imports. Parallel imports from much larger jurisdictions, such as the UK, have the advantage that they are sourced in larger and typically more competitive markets. In addition, parallel importing prevents suppliers from engaging in price discrimination to exploit differences in national markets.

### ***Potential remedies***

We have outlined three steps that could be considered in order to enhance competition in these markets, and to address the allegations of profiteering that occurred at the turn of the year in connection with the increase in the rate of impôts on tobacco. In many cases, these remedies would require changes to regulation of tobacco products, and so would involve the States of Jersey in balancing the potential for reductions in the difference in pre-tax prices of cigarettes with implications for the public finances or public health policy.

In order to facilitate parallel trade in tobacco products, the States of Jersey could:

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<sup>2</sup> Based on data sourced from Jersey Customs and Immigration Service (JCIS)

- a. Establish an agreement with other English-speaking territories in Europe (e.g. Gibraltar) regarding common packaging, thereby enabling importers and retailers to source tobacco products from those other territories, rather than being required to stock only Channel Islands packets – the adoption of a new Tobacco Directive by the EU next month, which will require pictorial warnings by 2016, might mean that this is an opportune time for such discussions to take place; or
- b. Establish an agreement with the UK and Isle of Man (possibly together with Guernsey), under which tobacco duty revenues would be pooled and shared, and tobacco products bearing the “UK Duty Paid” mark could therefore be sold in Jersey.

To address concerns regarding wholesalers and retailers engaging in “profiteering” at the turn of the year when the rate of duty typically increases, the simplest solution would be the development of bonded warehouses, with anti-avoidance rules similar to those already applied by HMRC in the UK.

## 1. Introduction

This market study into the supply of cigarettes and hand rolling tobacco (collectively, **tobacco products**) in Jersey was launched following a request from the Minister for Economic Development, Senator Alan Maclean (**the Minister**), under Article 6(4) of the Competition Regulatory Authority (Jersey) Law 2001 (**the Article 6(4) request**). The terms of reference for the study are discussed below in Section 1.1, and are contained in Appendix 1.

This study has focussed on the supply chain of duty-paid tobacco sold in Jersey. Using data collected from businesses that operate in each of the identified steps of the supply chain, the JCRA has analysed the proportion of the final retail price paid by customers that can be attributed to each step of the supply chain, and identified the gross margin earned by businesses in each section of the supply chain.

In addition, the JCRA has conducted the same analysis on the supply chain for the supply of tobacco in Guernsey and the UK. Using this information, the JCRA has been able to compare the margins earned by businesses involved in the supply of tobacco in Jersey with businesses operating a similar function in Guernsey and the UK.

### 1.1. Article 6(4) request

The Article 6(4) request outlined the following aims for the market study:

- To undertake a review of the level of pricing, costs and profit of tobacco products at the wholesale and retail level within Jersey.
- To produce a report on the level of competition in the tobacco market, with specific reference to exclusive supply agreements, making any such recommendations for change or improvement that might be considered.

The market study had the following scope:

- To compare the average wholesale and retail prices for cigarettes and hand-rolling tobacco sold in Jersey with prices charged in the United Kingdom and any other relevant jurisdictions based on available data;
- To give consideration to regulations in respect of the import and supply of cigarettes and hand-rolling tobacco in Jersey, as well as the States of Jersey Tobacco Strategy, and whether they impact on competition
- To consider and report on any other relevant matters that may arise during the course of the JCRA's review.

Discussion of the tobacco market and claims of profiteering preceded the Article 6(4) request.<sup>3</sup> Specifically, Senator Philip Ozouf raised concerns that tobacco wholesalers and retailers had been exploiting smokers by stockpiling cigarettes bought at the previous year's duty prices and selling them with the additional new duty added, pocketing the difference.<sup>4</sup>

In addition to this, the annual Retail Price Comparison reports published by the States of Jersey Statistics Unit compare prices for a range of products in Jersey, Guernsey and the United Kingdom. These reports over recent years have found that the mean retail price of cigarettes was lower in Jersey than in the UK, but that the pre-tax price in Jersey was substantially higher than in the UK.

Since June 2005, tobacco retail prices have risen steadily, with prices in June 2013 in Jersey having

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<sup>3</sup> Jersey Evening Post: *Minister's claim prompts full probe into tobacco marketing*, 15 January 2013.

<sup>4</sup> Jersey Evening Post: *Minister calls for prices probe*, 3 January 2013.

increased by 55%, UK prices by around 67% and Guernsey prices by approximately 49%. For the same period, general inflation in Jersey<sup>5</sup> was 27%, 26% in Guernsey<sup>6</sup> and 25% in the UK<sup>7</sup>.

A large proportion of the increase in these prices has been driven by increases in the duty levied on tobacco products. The Jersey duty rate (based on a packet of 20 cigarettes) saw an increase of 53% between 2005 and 2013, while the UK duty rate was raised by 58% and Guernsey's by 57% over that period.

The detailed calculations of the Statistics Unit with respect to comparative pre-tax and post-tax prices of cigarettes in the three jurisdictions are discussed in section 3.

## 1.2. Peculiarities of tobacco as a product

The heavy regulation of tobacco products makes them particularly unusual when considered alongside other fast moving consumer goods. There are few products whose consumption is actively discouraged by the state. For tobacco, this is done using a range of methods, including high duty rates, restrictions on where it can be consumed, who can buy it, how it is advertised and how it must be packaged.

These factors play a significant role in the competitive dynamics of the tobacco market. For example, the restrictions on how tobacco products can be advertised create significant barriers to entry into the tobacco market for new entrants, or for the development of new products more generally, because there are considerable restrictions on how the new entrant/product can advertise the fact that it has entered the market. Similarly, the packaging requirements applied by each territory are generally unique. This means that territories become unique markets and, because there is little chance of parallel imports being available, tobacco manufacturers are likely to have a greater ability to extract higher prices for their products than might otherwise be the case.

There is an inherent tension between the desire of public health authorities to reduce the availability and affordability of tobacco products, and the benefits of increased competition, including lower prices and greater availability. The States of Jersey Tobacco Strategy<sup>8</sup> (the **States Tobacco Strategy**), which is set out in Annex B of this report, has been implemented to reduce the incidence of smoking in Jersey through a number of measures, including reducing the availability and affordability of tobacco products. A 2013 report published by the Health Intelligence Unit of the States of Jersey highlighted the effect that smoking has on public health in Jersey and noted the increased incidence of cancers attributable to smoking in Jersey when compared to the South West of England.<sup>9</sup>

All other things being equal, it would be expected that higher prices for a product would lead to lower consumption. On this view, the fact that pre-tax prices for tobacco products are higher in Jersey than in the UK might be seen to be aligned with the policy direction of the States of Jersey, as formulated in the States Tobacco Strategy.

However, as the data analysis in this report shows, by far the largest influence on the price of tobacco products in Jersey, Guernsey and the UK (and well as most other jurisdictions) is the rate of impôts/duties. This variable is directly controllable by the States of Jersey in pursuit of its policy objectives. In the JCRA's view, the fact that the existing market structure might produce higher prices than would otherwise be expected in a more competitive market structure is not a sound

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<sup>5</sup> As measured by the retail price index. Jersey Retail Price Index: June 2012.

<sup>6</sup> As measured by the States of Guernsey inflation calculator: <http://www.gov.gg/RPIcalculator>.

<sup>7</sup> Using the RPI(J) index calculated by the Office for National Statistics, which is the closest comparator to Jersey RPI.

<sup>8</sup> The States of Jersey, *Tobacco Control Strategy 2010-2015*, 25 October 2010.

<sup>9</sup> Public Health England Knowledge and Intelligence Team, *Cancer in Jersey*, July 2013.



basis for failing to consider whether the market could operate more effectively.

In addition, it should be noted that this market study was requested by the Minister for Economic Development in light of the concerns outlined above. As such, we have conducted an analysis of the relevant markets and barriers to competition in a similar manner to any other of our market studies.

### **1.3. Assistance**

Many firms and States of Jersey Departments contributed to this study. Tobacco retailers, importers and manufacturers provided us with data, shared their experiences, and answered our questions. Information was also collected from a number of duty-free tobacco retailers. Many other organisations, such as the Public Health Unit of the States of Jersey, the Jersey Customs and Immigration Service (*JCIS*) and the States of Jersey Statistics Unit, were generous with their time, as was the States of Guernsey Customs and Excise Division. The JCRA is very grateful to all for their assistance throughout this study.

## 2. Market Characteristics

Understanding the structure of the Jersey tobacco markets is crucial to understanding the dynamics of the markets and why certain features of the markets exist. For tobacco products, market structure is heavily influenced by regulation and government policy.

In this section, we first review the regulation applied to tobacco products:

- The States Tobacco Strategy proposes three key areas for action and sets new and challenging targets for lowering the number of people smoking in Jersey, with the ultimate aim of realising the vision of a smoke-free Jersey.
- The packaging of tobacco products is highly regulated and often results in packaging becoming country-specific. We reviewed the packaging legislation in Jersey and compared it to that implemented in Guernsey and the European Union.
- For the general public, the most direct form of regulation of tobacco products is the levying of duty. In Jersey, and most other developed countries, duty generally accounts for at least 50% of the retail price consumers pay for tobacco products. We provide an overview of the form of that duty levied in Jersey, Guernsey and the UK.

Following the review of the regulatory landscape found in each jurisdiction under consideration, we then proceed to discuss the structure of the tobacco markets (duty-paid and duty-free) in each of those jurisdictions.

### 2.1. Regulation

#### 2.1.1. States Tobacco Strategy

In October 2010, the Council of Ministers endorsed a new Tobacco Control Strategy - a range of measures which aim to reduce harm caused by smoking in Jersey.

The strategy proposed the following three areas for action:

- Reduce the number of children and young people taking up smoking by:
  - i. Reducing the affordability of tobacco
  - ii. Reducing the availability of tobacco
  - iii. Increasing awareness of the harm caused by smoking
- Protect families and communities from tobacco related harm by:
  - i. Assessing and reviewing the evidence for extending smoke-free legislation to other public places and all motor vehicles
  - ii. Working with community groups to help people make their homes, cars and play spaces smoke free
  - iii. Working with Transport and Technical Services to reduce the unwanted effects of tobacco-related litter
- Motivate and assist every smoker to quit by:
  - i. Developing service level agreements with general practice and community pharmacists to extend the reach of the cessation service

- ii. Exploring opportunities for public-private partnership to deliver smoking cessation in the workplace
- iii. Developing and implement a marketing strategy to promote the smoking cessation service
- iv. Developing targeted cessation services for key groups such as pregnant women, ethnic minorities, mental health service users and prisoners

## 2.1.2. Tobacco packaging requirements

The combination of health warnings and fiscal marks currently required on Channel Island tobacco products is unique, simple substitution from another jurisdiction is not possible.

The current labelling requirements for tobacco products sold in Jersey are contained in the *Restriction on Smoking (Warning Notices) (Jersey) Regulations 2011* (the **Packaging Regulations**). A full copy of the Packaging Regulations can be found in Appendix 4.

The Packaging Regulations require packets of tobacco products to include specified written and pictorial warning notices and dictate the set of technical requirements relating to their appearance. Additionally, the Packaging Regulations require packets of cigarettes to include a statement of nicotine, tar and carbon monoxide yields. The Regulations set out the fifteen picture warnings that may adorn tobacco packaging sold in Jersey. Thirteen of the warnings are able to be sold in the domestic and travel markets. The remaining two are substitutes for each other. One carries details of the local quit smoking hotline and tobacco carrying this warning may only be sold in the domestic market. The alternate pictorial message that provides more generic information is provided for tobacco that is sold in the travel market.

The Packaging Regulations also state that tobacco sourced from Member States of the European Economic Area that comply with the labelling requirements of Article 5 of Directive 2001/37/EC (i.e. the existing Tobacco Directive) concerning the manufacture, presentation and sale of tobacco products shall be taken to comply the requirements set out in the Packaging Regulations relating to the size and technical requirements of the warning notices and yield statement. The content of the written and picture warnings must, however, be as set out in Regulation 2 and Schedule 2 of the Packaging Regulations.

This largely brings Jersey tobacco packaging requirements in line with those rules applied in much of the European Union (**EU**). However, the packaging requirements applied by the European Commission do not necessarily result in a single market for tobacco products within the EU and/or other countries implementing the EU standards. This is because the EU has a total of 24 official languages and each country requires that the text contained in the warning notices on tobacco packaging be printed in the predominant language/s spoken in the country in question. Moreover, pictorial warnings on tobacco packaging will only be compulsory from May 2016, following a new EU Tobacco Directive<sup>10</sup>.

Only three EU countries identify English as an official language: Ireland, Malta and the United Kingdom. Ireland and Malta have more than one official language (Gaelic and Maltese respectively). Warning labels in both countries must be printed in both official languages. Therefore, only tobacco destined for the UK market carries the same warning labels as tobacco products sold in Jersey.

The one area in which the packaging of UK tobacco differs from that of Jersey tobacco is the fiscal mark that Her Majesty's Revenue and Customs (**HMRC**) requires to be printed on all duty-paid

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<sup>10</sup> Council of the European Union, *Council adopts revised EU tobacco directive*, 14 March 2014 [http://www.consilium.europa.eu/uedocs/cms\\_data/docs/pressdata/en/lsa/141527.pdf](http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/lsa/141527.pdf)

tobacco sold in the UK. The fiscal mark is a label that must be carried on 'specified tobacco products' indicating that UK duty has been paid. It appears as a panel reading "UK Duty Paid" under the cellophane on packets of cigarettes and rolling tobacco.

The vast majority of commercial freight enters Jersey via the single commercial port, which allows JCIS to accurately identify and the flow of goods into the island. Because of this, JCIS is able to effectively monitor the importation of duty-paid tobacco in Jersey without the tobacco being duty stamped. Accordingly, tobacco imported into Jersey is not required to carry a fiscal mark to indicate that duty has been paid in Jersey. In addition, the interaction of health warnings and fiscal marks in various jurisdictions means that the Channel Islands packet for tobacco products is unique, and this also facilitates detection of smuggling.

Guernsey enforces the same packaging requirements as those enforced in Jersey.

### 2.1.3. Taxes

#### Jersey

Duty rates for tobacco products are set each year in the States of Jersey annual budget. New rates have historically come into effect on 1 January of the year in question. In Jersey, tobacco duty obligations are calculated based on the weight of the tobacco on which duty is being paid.

**Table 1: Tobacco Duty Rates in Jersey (2010-2014)<sup>11</sup>**

	2010	2011	2012	2013	2014
Cigarettes	£221.55/kg	£246.14/kg	£270.75/kg	£306.49/kg	£340.20/kg
Cigars	£177.17/kg	£196.84/kg	£216.52/kg	£245.10/kg	£272.06/kg
Hand rolling tobacco	£188.31/kg	£209.21/kg	£230.13/kg	£260.51/kg	£289.17/kg
Other processed tobacco	£171.48/kg	£190.51/kg	£209.56/kg	£237.22/kg	£263.31/kg
Leaf tobacco and other unmanufactured tobacco substitutes	£163.74/kg	£181.92/kg	£200.11/kg	£226.52/kg	£251.44/kg

On top of the duty that is levied on tobacco products, Jersey also levies a goods and service tax (**GST**) of 5% on goods and services sold in the island.

JCIS is responsible for monitoring goods that are subject to duties and collecting the duties due. It publishes quarterly statistics on the weight/volume of goods on which duty has been paid. The weight of duty paid tobacco products declared in Jersey annually between 2010 and 2013 is detailed in Table 2 below.

**Table 2: Weight of declared tobacco products subject to duty in Jersey<sup>12</sup>**

	2010	2011	2012	2013
Cigarettes	53,614.60kg	46,329.92kg	54,897.16kg	44,097.03kg
Cigars	365.06kg	285.4kg	219.59kg	208.56kg
Hand rolling tobacco	3,322.10kg	4,117.95kg	5,069.63kg	5,087.65kg
Other	209.32kg	112.2kg	89.84kg	99.32kg

<sup>11</sup> States of Jersey, JCIS, Duties payable in Jersey:

<http://www.gov.je/Government/Departments/HomeAffairs/Departments/CustomsImmigration/Traders/Pages/ExciseRate.s.aspx>

<sup>12</sup> Ibid

Between 2010 and 2013, cigarettes accounted for around 90% of all duty-paid tobacco products by weight consumed in Jersey. However, the amount of hand rolling tobacco being consumed has increased drastically over that period, increasing by 53% from 2010 to 2013. Over this period, cigarette imports have fallen overall, although the trend has varied from year to year.

## Guernsey

Tobacco products in Guernsey are taxed by the Customs and Excise Division using the same method as Jersey, i.e. based on its weight. Table 3 below displays the duty rates applicable in Guernsey for the period 2010 to 2014.

**Table 3: Tobacco Duty Rates in Guernsey (2010-2014)**

Duty Rates	2010 (20/11/09 - 11/11/10)	2011 (12/11/10 - 17/11/11)	2012 (18/11/11 - 13/12/12)	2013 (14/12/12 – 08/10/13)	2014 (09/10/13 -
Cigarettes	£210.69/kg	£220.38/kg	£234.70/kg	£251.13/kg	£265.44/kg
Hand Rolling Tobacco	£182.18/kg	£190.56/kg	£202.95/kg	£217.15/kg	£229.54/kg

Source: Guernsey Customs and Excise

Unlike Jersey, Guernsey’s excise rates are not applied on a calendar year basis. New duty rates have generally been enforced for 12 month periods, with the duty rates typically being changed in November. The exact dates during which the duty rates were in force are presented in brackets in the table above.

Unlike Jersey, the States of Guernsey do not levy a general tax on goods and services.

Table 4 below, details the total weight of duty paid cigarette and hand rolling tobacco products that entered the market in Guernsey between 2010 and 2013.<sup>13</sup>

**Table 4: Total Weight of Duty-Paid Tobacco Products in Guernsey**

Imports (kg)	2010	2011	2012
Cigarette	31,931.03kg	30,770.06kg	28,711.79kg
Hand Rolling Tobacco	4,369.76kg	4,040.74kg	4,282.19kg

Source: Guernsey Customs and Excise

## United Kingdom

Duty on cigarettes is calculated in the UK on a different basis to tobacco products in the Channel Islands.

In the UK, duty on cigarettes is calculated using the following two step method:

- **ad valorem duty:** a percentage of the retail price, including VAT and specific duty; and
- **specific duty:** a fixed amount per 1000 cigarettes

The retail price is taken as the manufacturer's or importer's recommended retail selling price in force at the time the cigarettes become chargeable with duty. That price must include all duties and taxes. No deduction from the price may be made for:

<sup>13</sup> The time periods in Table 4 refer to the time periods referenced in Table 3.

- any token, coupon, card, etc., in a packet, or
- any special offer or reduction unless this applies to all cigarettes of that description and HMRC is satisfied that it constitutes a genuine change in the recommended selling price.

Manufacturers have provided the JCRA with the recommended retail price for all cigarette varieties considered in this market study and it is with these prices that the JCRA has calculated the value of the ad valorem duty attributable to each cigarette variety analysed. Duty levied on rolling tobacco in the UK is calculated based on the weight of the product, similar to the method used in Jersey and Guernsey.

On top of duty, the UK levies a value added tax of 20% on all goods and services sold in the UK (with the exception of domestic fuel which has reduced VAT of 5% and children’s clothes and most food products, which are zero rated). Table 5 lists the duty rates in force in the UK between 2009 and 2013.

**Table 5: UK Tobacco Duty Rates<sup>14</sup>**

Duty Rates		22/04/09 - 23/03/10	24/03/10 - 22/03/11	23/03/11 - 20/03/12	21/03/12 - 19/3/13	20/03/13 -
Cigarettes	Ad valorem	24% of RRP	24% of RRP	16.5% of RRP	16.5% of RRP	16.5% of RRP
	Specific (per 1000 sticks)	£114.31	£119.03	£154.95	£167.41	£176.22
Hand Rolling Tobacco (per Kg)		£124.45	£129.59	£151.90	£164.11	£172.74

Because the HMRC levies duty on a per cigarette basis, rather than using the weight-based method applied in the Channel Islands, tobacco duties received by HMRC are recorded on a per cigarette basis. This is reflected in the HMRC *Tobacco Bulletin*, which provides data a range of metrics related to tobacco duties in the UK, including the quantities of tobacco products released for consumption and the current and historic tobacco duties rates.

Table 6 below, which details the total weight of duty-paid cigarettes in kilograms, has been calculated by converting the total number of duty-paid cigarettes released into the UK market into a weight-based measure. To do this, the average weight of Channel Islands cigarettes, as provided by manufacturers for the calculation of duty liability, has been used as an approximation. The average weight of this sample is 648.7gms per 1000 sticks, with a variation of 3.4gms. As such, the figures provided in Table 6 should be considered to be indicative of the relative sizes of the markets in Jersey, Guernsey and the UK, rather than as conclusive evidence of the market size in the UK.

**Table 6: Approximate Weight of Duty Paid Tobacco Entering the UK Market<sup>15</sup>**

Weight of duty paid tobacco products (kg)	2010	2011	2012	2013
Cigarettes	29,343,945 kg	27,236,318 kg	26,236,023 kg	23,259,787kg
Hand Rolling Tobacco	5,378,000 kg	5,850,000 kg	6,290,000 kg	6,314,000kg

## 2.2. Market Structure

The JCRA has sought information from a range of parties involved with the supply of tobacco products in Jersey, Guernsey and the UK. This includes manufacturers, importers and retailers. The supply chains for the Channel Islands and the UK are depicted below, and described in more detail in

<sup>14</sup> HMRC, Tobacco Bulletin February 2014.

<sup>15</sup> HMRC, Tobacco Bulletin February 2014. These figures relate to the calendar year.

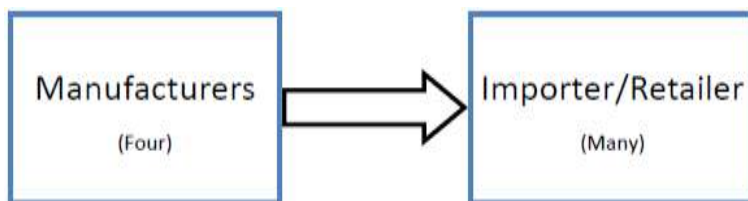
the following section.

### *Channel Islands*



\* As noted earlier, Gallaher owns the trademarks for the Silk Cut and Benson & Hedges brands in the EU. In the Channel Islands, the trademark for these brands is held by BAT.

### *United Kingdom*



## **2.2.1. Jersey**

The overwhelming proportion of cigarette and rolling tobacco products consumed in Jersey are supplied by three manufacturers, Philip Morris Limited (**PMI**), British American Tobacco UK Limited (**BAT**) and Imperial Tobacco Limited (**Imperial**).

J.J. Fox Trading Limited (Jersey) (**J.J. Fox**) and Longueville Distributors Limited (**Longueville**) are the two major importers of tobacco products in Jersey.<sup>16</sup> J.J. Fox imports products of PMI and BAT, while Longueville, a subsidiary of The Liberation Group, imports products of Imperial.

The JCRA has taken steps to ensure that none of the data published in this market study can be backwards-induced in a manner that generates meaningful data. However, because the information that has been provided to the JCRA by the retail businesses is highly confidential and commercially sensitive and there is little benefit in publishing the identity of the retail businesses that have provided information, the JCRA has elected not to publish the identities of the retail businesses or number of retail businesses that have provided data in question, in order to provide the retail data presented in this market study with additional protection.

For duty-paid tobacco sold in Jersey, the supply chain has three or four stages. Tobacco products are produced by the manufacturer. When the tobacco is appropriately packaged, the tobacco is delivered to the importer's warehouse by the manufacturer. The two primary importers use different business models. Of the two importers, J.J. Fox offers a much more comprehensive distribution network and plays an active role as not only an importer of tobacco, but also a distributor of tobacco products to retail outlets. Longueville, on the other hand, plays only a small role in the distribution of tobacco products to retailers and with the exception of the large established retailers (such as supermarkets), sells its products primarily to local distributors, who then distribute the goods to retailers. In both cases, the importer is responsible for the payment of the duty liability that is incurred by importing the tobacco to Jersey.

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<sup>16</sup> There are an additional two cigarette and/or rolling tobacco importers in Jersey that have not been included in this market study because their combined impact on the Jersey market is very small.

There are three primary tobacco manufacturers represented in the Jersey market: BAT, PMI and Imperial. Globally, there are four major tobacco manufacturers, the fourth being Japan Tobacco International (*JTI*). JTI only sells two brands of tobacco products in Jersey, Mayfair King Size and Mayfair King Size Smooth, and these two products account for a small proportion of the market. JTI's presence in the Jersey market is small due to a trademark agreement between JTI and BAT, under which JTI owns the trademark for the Benson & Hedges and Silk Cut brands in the EU and BAT holds the trademark for the same brands in a number of other jurisdictions, including the Channel Islands. As a result, the majority of tobacco products supplied to the Jersey market are supplied by three of the four major tobacco manufacturers.

The logistics involved in delivering tobacco products to Jersey dictates that order volumes must be large enough to justify the freight costs. In addition, because tobacco destined for the Channel Islands have unique packaging, manufacturers must undertake a specific run to fill the order that has been placed. There are costs involved with such runs, and the smaller a run, the smaller the number of packs across which production costs can be spread. Moreover, we are told by the importers that due to the high production costs associated with small production runs, it has become uneconomic to maintain sales of certain brands in the Channel Islands, resulting in many brands being delisted in recent years.

Unlike larger markets such as the UK, tobacco manufactured for Jersey is manufactured to order rather than manufactured to stock. In large jurisdictions in which manufacturers have a range of customers, the manufacturer estimates the volume that the entire market will require and uses this stock to fulfil orders that are received. In Jersey, manufacturers have only one customer and therefore manufacture product based on that one customer's order. Because the entire run of a product is manufactured based on that one customer's order, the customer is required to purchase the entire volume of the order, irrespective of any changes in circumstance between the date the order is placed and the date the order is manufactured, which can in some instances be a significant length of time. It is these dynamics that dictate that orders placed by Jersey importers need to be carefully planned to ensure that sufficient stock is held to satisfy demand for the period between order deliveries.

The retail market consists of a wide range of retail outlets - from large supermarkets, to convenience stores, to pubs and bars.

### **2.2.2. Guernsey**

Guernsey has a similar market structure to that found in Jersey. The same three tobacco manufacturers provide the significant majority of tobacco products to the Guernsey market. Again, only two importers are present in Guernsey and both are subsidiaries or trading arms of the same importers represented in Jersey for the same tobacco manufacturers.

As in Jersey, one of the importers has a more prominent role in distributing tobacco across the island to retailers and the other only distributes to large buyers. However, in Guernsey, it is Bucktrouts (a Liberation Group subsidiary) that engages in significant product distribution. Outside of a few large buyers, J.J. Fox Guernsey offers no distribution services. As in Jersey, the importer is responsible for the payment of any duty due on the imported tobacco.

### **2.2.3. United Kingdom**

The four manufacturers referenced in the paragraphs above (PMI, BAT, Imperial and JTI<sup>17</sup>) are all active in the UK tobacco market. The distribution mechanism for tobacco products in the UK is

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<sup>17</sup> JTI's UK trading company is Gallaher Limited



different and considerably more varied than in the Channel Islands; in part, a product of the relative complexity of the market in the UK.

In the UK, the manufacturers have an array of customers, rather than the single customer each manufacturer has in Jersey. In the UK, manufacturers typically have direct supply relationships with many large retail customers such as supermarkets. For customers that do not maintain a direct relationship with the manufacturers, products can be sourced from various distributors who themselves have direct relationships with manufacturers. Smaller retailers, for whom a direct relationship would not be economic, and larger retailers that elect not to purchase tobacco from the manufacturers, source their tobacco direct from one of these distributors.

As with the importers in Jersey, the JCRA understands that tobacco products are delivered by the manufacturer directly to the premises of the purchaser. The purchaser then distributes the product to their stores, if they are a retailer, or to the various stores of their clients, if they are a distributor.

#### **2.2.4. Duty-free market**

Anecdotal evidence from a range of sources has suggested that tobacco purchased duty-free accounts for a significant proportion of the volume of tobacco products consumed in Jersey. Most estimates range between 40% and 50% of overall consumption.

The current duty-free allowances for a single passenger entering Jersey are 200 cigarettes or 250g of other tobacco products. JCIS intercepts annually several hundred passengers that have exceeded their import allowances for tobacco. However, monitoring duty-free limits is not as high a priority of JCIS as intercepting prohibited goods (e.g. narcotics), so the risk of being found to have exceeded the duty-free limit is small and there is little incentive for passengers to ensure they comply with the duty-free allowance limits. If caught, a range of penalties can be imposed by JCIS depending of the severity of the offence. These penalties range from requiring the passenger to pay the value of the excess duty to prosecution.

The nature of the transport links means that there are a large range of retail outlets from which duty-free tobacco consumed in Jersey may originate. Jersey Airport currently lists 48 destinations from which it is possible to travel to Jersey<sup>18</sup>. When added to the six locations from which it is possible to travel to Jersey by boat (Poole, Portsmouth, Weymouth, Guernsey, St Malo and Granville), there are 54 locations with transport links that terminate in Jersey.<sup>19</sup>

The JCRA understands that only four of the 48 locations from which air passengers can travel to Jersey do not offer duty-free shopping. In addition to this, the significant majority of air passengers travelling to Jersey are also offered the opportunity to purchase duty-free products in-flight, providing most passengers with two options to purchase duty-free goods. Additionally, Condor Ferries, the carrier of the significant majority of sea passengers to Jersey, sells duty-free products on-board. Duty-free goods are not available to incoming passengers (air or sea) in the airport or ferry terminal in Jersey. Passengers wishing to bring duty-free goods into Jersey must purchase the goods either at their departure terminal or on board their vessel/aircraft.

Collecting data on volume of duty-free tobacco products entering Jersey from each of the 54 locations with transport links that terminate in Jersey would require an enormous investment of time and resources to ensure the data collected is accurate. However, the JCRA has contacted transport operators (air and sea) that account for a significant proportion of international passengers entering Jersey and collected data on the prices at which they purchase duty-free tobacco and the prices at which they sell the same products. From the information provided, the

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<sup>18</sup> Six of these locations are served by charter flights.

<sup>19</sup> There may, of course, be more.

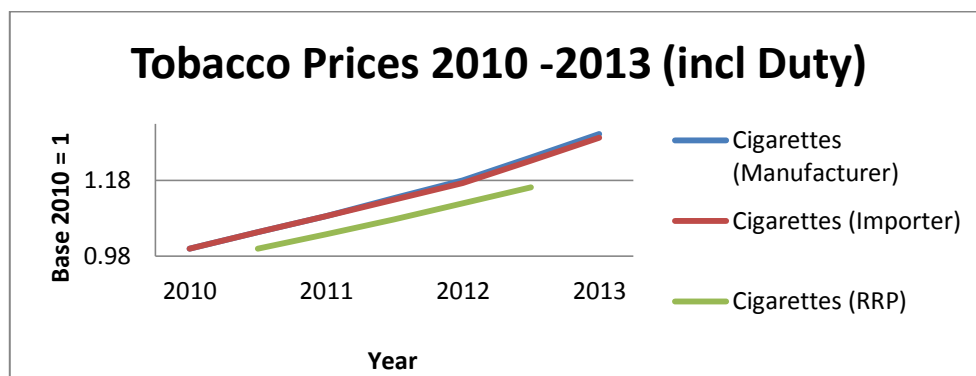
JCRA has identified that most products are generally procured directly from the manufacturer, although there is a small proportion of products that some operators procure from wholesalers.

### 2.3. Price trends

Prices for tobacco products, both including and excluding duty, have risen significantly over the last three years, with over half of the increase due to higher levels of duty.

Data provided by the manufacturers and importers allows us to show the evolution of the price charged at each step in the Jersey supply chain for cigarettes between 2010 and 2013. We have not collected retail prices for the entire period, so the figures that follow do not represent the actual prices encountered in the market during this period. As a proxy for this, we have used the manufacturers' recommended retail prices (*RRP*).

**Figure 1: Jersey Cigarette Price Index: 2010 – 2013 (including Duty)**



Due to a mismatch between the time periods for which the data above applies, the RRP data does not cover the same time period as the manufacturer and importer data. The manufacturer and importer data covers the period calendar years for 2010 to 2012, while the 2013 data relates to the first quarter. The RRP data does not relate to calendar years, but overlaps between 2010/2011 to 2012/2013. As a result, the time series of the data sets do not match exactly.

Figure 1 demonstrates that the prices charged by manufacturers and importers have increased by very similar rates over the time period in question, approximately 30%. A significant proportion of this increase can be attributed to the annual increases in Jersey tobacco duty. Between 2010 and 2014, the duty applied to cigarettes has increased by 54%, from £221.33/kg to £340.20/kg.

In Figure 2 below, the duty element has been removed from the prices.

**Figure 2: Jersey Cigarette Price Index: 2010 – 2013 (excluding Duty)**

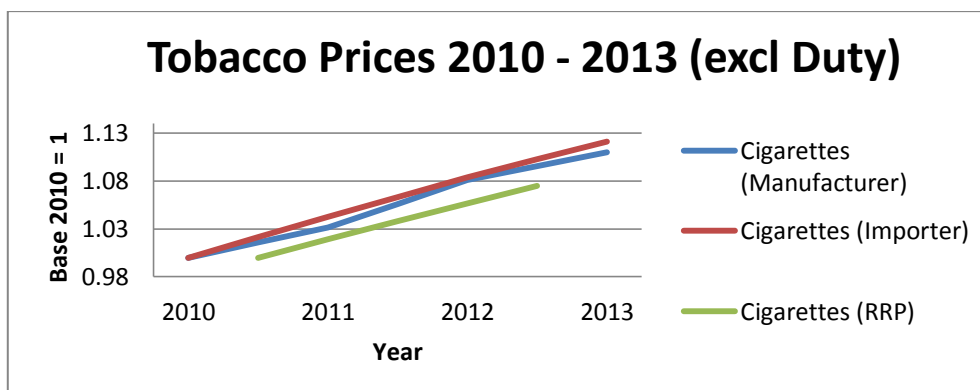


Figure 2 indicates that increases in duty are responsible for over half of the total increase in prices between 2010 and 2013.

As in Figure 1, the price increases of manufacturers, importers and RRP follow similar paths. The manufacturer prices and the corresponding importer prices appear to have increased by approximately 11%-12% between 2010 and 2013. It is important to note that the price paid by importers to manufacturers for wholesale cigarettes accounts for 78% of the price charged by importers to retailers. The remaining 22% of the price at which importers sell cigarettes is accounted for by rent, wages, equipment, profit etc. The majority of these costs are Jersey-specific and typical, or expected, increases in these costs could be explained by the retail price index calculated by the Statistics Unit.

Over the 2010–2013 period, the Jersey retail price index increased by approximately 9.5%. If the factors responsible for the other 22% of the price charged by importers not attributed to the cost of purchasing cigarettes from manufacturers increased at the same rate as RPI, we would expect the increase in importers' prices to be less than that of manufacturers' prices, not more. However, RPI is an aggregate calculation and does not necessarily exactly reflect the evolution in the costs of importers between 2010 and 2013. We do note that the increase in RPI is not significantly dissimilar to the price increases observed and that an increase above those exhibited by the manufacturers' prices of one or two significant importer costs could explain the difference.

### 3. Analysis of prices, costs and margins

In this section, we provide a summary of the process we have followed when collecting data on the tobacco markets in Jersey, Guernsey and the UK. A more comprehensive account of the data collection process is provided in Appendix 3.

Analysis of the data collected is then conducted and we attribute the proportion of the final retail cost of tobacco products to each step of the supply chain in each jurisdiction.

This allows us to identify not only the major contributors of the retail price, but also compare the proportion that each level of the supply chain contributes to the final price across the jurisdictions.

#### 3.1. Data collection

Using the data collected from retailers, importers and manufacturers, we have been able to calculate the proportion of the total retail price that can be attributed to each step in the supply chain (and duty/GST/VAT). To do this, we collected data from manufacturers, importers and retailers in Jersey, Guernsey and the UK.

In Jersey and Guernsey, information has been sourced from manufacturers, importers and retailers (that purchase directly from the importers). In the UK, many large retailers purchase their tobacco directly from the manufacturer and it is from retailers that have this arrangement that the JCRA has collected its data.

The JCRA identified retailers with a presence (either directly or through affiliates) in Jersey, Guernsey and the UK. The JCRA requested data on the retailers' top ten selling cigarette stock keeping units (**SKUs**)<sup>20</sup> and top two selling hand rolling tobacco SKUs in Jersey. Having established each retailer's top ten/two selling SKUs, the JCRA requested each retailer to provide data on the same twelve SKUs relating to the retailer's operations in Guernsey and the UK. Seven cigarette products and two rolling tobacco products feature in the list of every retailer surveyed. It is the data on these nine products that the JCRA has used to attribute the final cost of a cigarette or rolling tobacco to each step in the supply chain.

For the purposes of this market study, the supply chain in the Jersey and Guernsey consists of the tobacco manufacturers, the importers, and retailers. In the UK, the supply chain analysed consists of the tobacco manufacturers and the retailers.

The "manufacturer price" has been defined as the price paid (net of VAT/GST and duty) by the importers, in Jersey and Guernsey, and the retailers in the UK, to the manufacturers of the tobacco products.

In the Channel Islands, the "importer margin" is defined as the difference between the price paid for products from the manufacturers and the price at which the product is sold to retailers. The "retail margin" is defined as the difference between the price retailers pay to purchase products from importers and the price at which the products are sold in the retail market.

The definitions are similar for the UK. However, in the UK, the retailer effectively undertakes the functions of the importer and the retailer in the Channel Islands. For the purposes of comparison with the supply chain found in the Channel Islands, the difference between what retailers pay the manufacturer for tobacco products and the price at which same tobacco products are sold by retailers to retail customers is defined as the "importer/retailer" margin.

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<sup>20</sup> A stock keeping unit is a number or string of alpha and numeric characters that uniquely identify a product.

In terms of the manufacturer price and the importer margin, there are two sources of data that can be used: the buy-side and the sell-side. For example, the manufacturer price can be calculated by using the price that importers state they pay for tobacco products or the price at which manufacturers state that they sell tobacco products to importers. In theory, these prices should be identical.

Due to the refusal of PMI and JTI (the supplier of Silk Cut and Benson & Hedges brands in the UK) to provide data on the prices that they charge in the UK and our desire to avoid protracted legal debate regarding the reach of Article 27 of the Competition (Jersey) Law 2005<sup>21</sup>, we have been unable to conduct this cross-check on the manufacturer price in the UK. Because we have not received the full set of data from the manufacturers, we have decided to use only the data provided by the retailers in the UK to determine the manufacturer price.

It is important to emphasise that the term “margin” in this analysis does not refer to profit. References to margin are simply to the price at which a good is sold, less the cost price of the goods. It does not account for other costs, such as rent, wages, overheads etc.

We have not endeavoured in the course of this market study to analyse the profits of those involved in the supply chain for tobacco products in Jersey, but have instead focussed on differences in prices. Calculations of profit are highly vulnerable to assumptions regarding costs. Moreover, many of the businesses in this supply chain supply a wide range of products other than tobacco, and so identifying profits that are referable to tobacco would be extremely complex, and potentially arbitrary.

### 3.2. Netback Analysis - data

Using the data sourced from parties through the data request set out in Annex B, the following analysis has been prepared for the average price of a pack of 20 cigarettes in Jersey, Guernsey and the UK, as well as at duty-free retailers serving passengers travelling to Jersey.

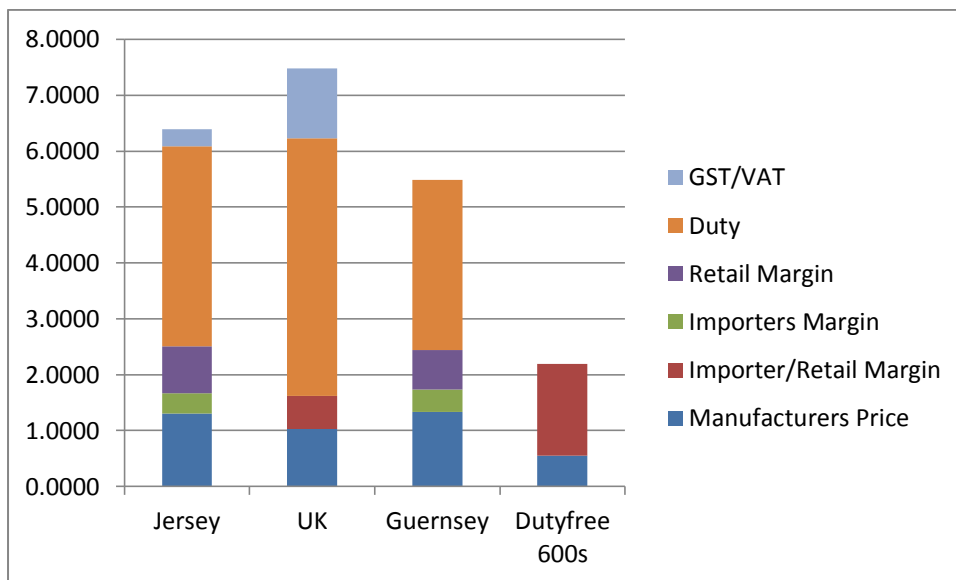
The data is a simple average of the seven of the top ten brands in the Channel Islands that were sold by the providers of the data in each of the three jurisdictions. The data was submitted on a monthly basis for the period from April 2012 to March 2013, as a simple average of each of the 12 monthly data points. As such, the retail prices quoted reflect duty rates applicable in 2012 and 2013. Given, in particular, that duty rates have increased in each of the jurisdictions since that time, the prices quoted do not reflect the retail prices of cigarettes as at the date of this report.

**Table 7: Breakdown of components attributable to Final Retail Price of a pack of 20 Cigarettes (£)**

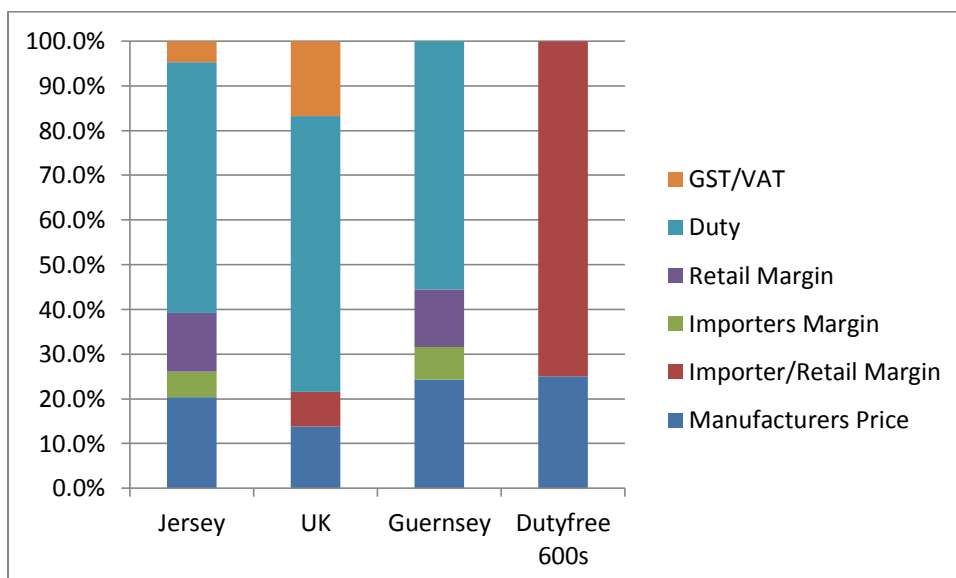
	<b>Manuf. Price</b>	<b>Importer Margin</b>	<b>Retail Margin</b>	<b>Pre-tax Price</b>	<b>Duty</b>	<b>GST / VAT</b>	<b>Retail Price</b>
<b>Jersey</b>	1.30	0.37	0.84	2.51	3.58	0.30	6.39
<b>UK</b>	1.03	0.59		1.62	4.62	1.25	7.49
<b>Guernsey</b>	1.33	0.40	0.71	2.44	3.05	0	5.49
<b>Duty-free 600s</b>	0.55	1.64		2.19	0	0	2.19

<sup>21</sup> Article 27 of the Competition (Jersey) Law 2005 provides the JCRA with the authority to require the provision of information and documents.

**Figure 3: Breakdown of components attributable to Final Retail Price of Cigarettes (£)**



**Figure 4: Breakdown of components attributable to Final Retail Price of Cigarettes (%)**



### 3.3. Netback analysis - commentary

Table 7 shows that, net of tax and duty, cigarettes in the duty-paid market in Jersey are on average 89p per pack (or 55%) more expensive than in the UK, and 7p per pack more expensive than in Guernsey. The contributors to that higher pre-tax price are across the supply chain: higher prices charged by manufacturers add 27p per pack, while differences in the gross margin attributable to import and retail activities add 62p per pack, relative to the UK. Interestingly, when compared to Guernsey, the importer margin is 3p per pack lower in Jersey, while the retailer margin is 13p per pack higher.

The JCRA estimates that approximately 3.9 million packs of 20 cigarettes are sold annually in the duty-paid market in Jersey. Our analysis of price differences therefore suggests that consumers in

Jersey pay approximately £3.4 million more annually for cigarettes in the duty-paid market than they would if cigarettes were priced on a pre-tax basis at the same level as in the duty-paid market in the United Kingdom.

Some differences in the “margins” can be explained by the higher cost of doing business in Jersey (and Guernsey). Importers cite higher staff and warehousing costs and regulatory compliance costs, amongst others. However, in our view, it is likely that these can only explain a small proportion of the difference. This is particularly borne out by the fact that differences in pre-tax retail prices between the UK and Jersey for certain other non-perishable goods are considerably less.

The JCRA considers that the 55% difference in pre-tax prices between Jersey and the UK is significant. While some of the price difference may be attributable to transporting the product to Jersey, cigarettes are compact and lightweight, particularly relative to their value, and can be transported as ambient freight, and this should be reflected in the freight charges. It should be noted that the pre-tax difference between prices in Jersey and the UK for cigarettes is considerably higher than for most other types of consumer goods. The Retail Prices Comparison by the States Statistics Unit found that price differences between the UK and Jersey for products such as meat (16%), fruit (42%) and vegetables (30%) are lower than for cigarettes, despite the fact that those products are bulkier than cigarettes and require refrigerated freight.

It should be noted that despite the significant percentage difference in pre-tax prices between Jersey and the UK, it remains the case that duty and GST makes up more than 60% of the retail price of cigarettes in the netback analysis – this figure will have increased subsequently, with a further substantial increase in tobacco duty at the start of 2014.

We have set out comments on the findings for each level of the supply chain below.

### ***Manufacturer prices***

There is a significant difference, 27p per pack of 20, or 26%, between the prices that manufacturers charge UK retailers for cigarettes and the prices charged to the importers in Jersey. This difference accounts for about one-third of the overall difference in pre-tax price between the UK and Jersey. Based on this analysis, tobacco manufacturers charge more than £1 million extra every year for supplies to the duty-paid market in Jersey than they would if they had charged average UK duty-paid prices.

Manufacturers have stated that there are a number of reasons why the cost of manufacturing and supplying tobacco for the Jersey market is more costly than manufacturing and supplying tobacco for the UK market. Principally, manufacturers state that only small production runs are required to satisfy demand in Jersey and Guernsey (given the unique Channel Islands tobacco packaging) and that they are therefore unable to realise the same manufacturing economies of scale as can be achieved when manufacturing product for larger markets. Other factors such as logistics costs and different legal and tax regimes have been provided as reasons for differences in the cost of producing tobacco for the Jersey and other markets.

As part of the information request sent to all manufacturers, the JCRA invited all manufacturers to present any views that they had on matters falling within the study’s terms of reference. The manufacturers provided assertions that the manufacturing costs are different but presented no concrete evidence, which makes it difficult to test these claims.

However, there is other evidence which suggests that manufacturers may have a degree of market power in deciding the level at which to set the prices charged in particular jurisdictions:

- Table 7 includes data for duty-free cigarettes supplied by Jersey-based vendors. The

manufacturer price per pack of 20 cigarettes was just 55p, less than half the average cost in Jersey (although it should be noted that the duty-free calculation was based on a carton of 600 cigarettes, and it is not uncommon for discounts to apply for larger-sized packs in consumer goods markets). Also, the delivery costs for these packs is likely to have been similar to the costs borne by manufacturers in delivering to the Channel Islands (since most of the duty-free retailers included in the sample are located in, or based in, Jersey or Guernsey).

- The average manufacturer price of one of the top brands of rolling tobacco is actually significantly cheaper in Jersey than in the UK. Rolling tobacco supplied in the duty-paid market in Jersey faces the same small production runs as cigarettes, since the packaging is specific to the Channel Islands. However, this appears not to be a factor in pushing up the price charged by the manufacturer for this particular brand.

### ***Importer/retailer margins***

Combined importer/retailer margins in the Channel Islands are significantly higher than the retail margin in the UK. The margin in Jersey, at £1.21 per pack, is more than double the retailer margin observed in the UK, at 59p per pack. This aspect of the supply chain accounts for 62p of the total 89p difference in pre-tax pack prices (approximately two-thirds of the difference). Indeed, the retail margin alone in Jersey, at 84p, is more than the retail margin in the UK, at 59p, despite the fact that retailers in Jersey typically carry out fewer of the distribution functions for tobacco products than their counterparts in the UK.

As noted in section 2.2, the distribution chain for tobacco products in the Channel Islands is different to that in the UK. While large retailers in the UK deal directly with manufacturers, all tobacco products sold in the duty-paid market in Jersey and Guernsey are handled by importers. In that sense, some of the functions carried out by importers in the Channel Islands (storage, transport of products to individual stores) are typically undertaken by the retailer in the UK. Therefore, for the purposes of comparison, we have taken importer and retailer margins in the Channel Islands, and analysed them against retailer margins in the UK.

Retailers of tobacco products in the Channel Islands have noted that while the retailer margin is high relative to the UK, it is not necessarily high compared to retailers' margins on other categories of groceries.

It is difficult to explain the apparently high margins in retailing. Of all of the stages of the Jersey supply chain for tobacco products, it has the conditions that would seem to be closest to a reasonably competitive market; in particular, the existence of many competitors (Waitrose, Iceland, Co-op, Spar, Checkers Express, other corner stores, specialist tobacconists, petrol forecourts). The reasons for the likely lack of competition at the retail level are explored further in section 4.3.

The large difference between the retail margin in Guernsey (71p) and Jersey (84p) is strange, given that the stock is likely to be sourced from the same importer, and most retailers operate across both islands (and so presumably have similar pricing policies). It was suggested to us by one retailer that the explanation could be that it and some other retailers apply a percentage mark-up to the wholesale cost of tobacco products. Given that the wholesale cost of cigarettes is significantly lower in Guernsey than Jersey (due to lower rates of tobacco duty and the absence of GST), a common percentage retail mark-up across both islands (e.g. 15%) would produce a lower absolute retailer margin in Guernsey.



### 3.4. Alternative price comparisons

There are alternative estimates of the average difference in the pre-tax price of packets of cigarettes between the UK and Jersey: from the States Statistics Unit in its annual Retail Price Comparisons publication, and from an importer of tobacco products to Jersey. Both other analyses show a lower difference between Jersey and UK prices than the data reported in section 3.2. This section will outline the methodological and data differences in the three approaches, and examine the strengths and weaknesses of each approach.

The States Statistics Unit has reported on comparisons of the retail prices of a range of consumer goods in Jersey, Guernsey and the UK for several years. When reporting on the retail prices of road fuel, alcohol and tobacco products, the Unit typically compares both pre-tax and post-tax prices, in part because duties make up such a significant portion of these products, but also because duty rates can vary significantly between Jersey, Guernsey and the UK. Historically, duty rates on petrol, alcohol and tobacco products were considerably lower in Jersey and Guernsey than in the UK, so post-tax retail prices were lower. However, the comparison has usually shown that when taxes and duties are removed, pre-tax retail prices in Jersey for these products are higher than in the UK.

For a packet of 20 cigarettes, the Unit has reported average differences in pre-tax retail prices between the UK and Jersey as follows:

**Table 8: Pre-tax and post-tax prices of a pack of 20 Cigarettes in the UK and Jersey<sup>22</sup> (£)**

Year	2000	2005	2009	2010	2011	2012	2013
UK retail price	3.96	4.57	5.45	5.88	6.58	7.11	7.77
Jersey retail price	2.81	4.58	5.44	5.23	5.55	6.27	6.80
UK pre-tax retail price	0.69	0.84	1.25	1.33	1.42	1.40	1.67
Jersey pre-tax retail price	1.41	1.78	2.13	1.93	1.79	2.13	2.18
Extent pre-tax prices are higher in Jersey than UK	0.72	0.94	0.88	0.60	0.37	0.73	0.51

The Jersey data used by the Unit is sourced from its own retail prices survey for the calculation of the Jersey Retail Prices Index, while the UK data is sourced from its counterpart in the United Kingdom, the Office for National Statistics. The statistics relating to tobacco products have been the subject of dispute in the past between the Unit and importers and retailers of tobacco products in Jersey. The Unit uses matched brands in its analysis, but notes that “the effect of the different consumption distributions of premium, mid-range, value for money (vfm) and sub-vfm brands in the two jurisdictions is to increase the mean retail and pre-tax prices for Jersey relative to the UK”.

The data used by the States Statistics Unit for this publication relates to a relatively short time period (June), whereas the figures in section 3.2 cover a 12 month period. As such, the analysis by the Unit might be affected by the timing of wholesale price changes, whereas the data in section 3.2 should

<sup>22</sup> Source: *Retail Price Comparison Reports* (various years), States Statistics Unit. Note that this data covers several editions of the retail price comparisons report, and the methodology used by the States Statistics Unit may have evolved over time.

not be affected by that factor. The data in section 3.2 is based on seven of the ten highest selling cigarette brands in the Channel Islands, whereas the analysis by the Statistics Unit covers a different range of brands. Moreover, the data used by the Unit covers a wide range of retailers in the UK, whereas, because of the difficulties in collecting data from the UK tobacco manufacturers and certain refusals to respond to JCRA information requests (see Appendix 3 below), the UK data cited in this report has been gathered from a smaller number of retailers. The data published by the States Statistics Unit looks only at the retail price, and so cannot show the division of the purchase price into the various supply chain components.

The importer provided a calculation of the difference between Jersey and UK cigarette prices for one of its well-known brands (which is also one of the seven brands included in the analysis in section 3.2). The difference in pre-tax price was 49p per packet of 20 cigarettes (that is, Jersey pre-tax prices were 27% higher than in the UK). Relative to the average calculation in this report of 89p per packet, the Jersey pre-tax price was 21p per packet lower, while the UK price was 19p per packet higher.

The calculation by the importer covers only one brand of cigarettes, whereas the JCRA analysis above includes seven brands, a portion of which are carried by each of the respective Jersey importers. In addition, the UK prices used for the importer's calculation are the manufacturer's recommended retail price. By contrast, the data cited in this report are based on the *actual* prices charged by the relevant retailers.

## 4. Barriers to competition

The netback analysis outlined in section 3 suggests that margins at each level of the tobacco supply chain – manufacturing, importing and retailing – are considerably higher in the Channel Islands than in the UK. There are two particular features of the structure of the market for tobacco products in Jersey which limit competition and may contribute to the significantly higher pre-tax price of tobacco products in Jersey relative to the UK:

- **Parallel importing is impossible** - The combination of packaging legislation and duty rules in the UK means that parallel imports of tobacco products to Jersey from the UK (or, indeed, any other territory) are essentially impossible.
- **Exclusive agreements in place** - JJ Fox and Longueville have exclusive agreements with the manufacturers who supply to them, so no other companies can import their products to the Channel Islands. By contrast, in the UK, large retailers will typically deal directly with tobacco product manufacturers, rather than third-party distributors.

These features in turn are likely to have an impact on the extent of competition at the retail level, and this is discussed separately in this section as well.

### 4.1. Absence of parallel imports

The only material difference between Jersey tobacco packaging and UK tobacco packaging is the presence of the UK fiscal mark. However this difference makes parallel importing of tobacco products essentially impossible.

This inability to engage in trade, and to source products from other more competitive markets, gives importers of tobacco products in the Channel Islands an almost unique degree of protection from competition. The only other consumer product in respect of which parallel trade between the UK and Jersey is impossible (other than through the possession of a licence) is cows milk in liquid form, and that protection is the result of an explicit policy decision of the States of Jersey through the *Customs and Excise (Import and Export Control) (Jersey) Order 2006*. Set out below is a brief explanation of how the interaction of the requirements of Jersey and UK legislation prevents parallel trade in tobacco products.

As noted above in section 2.1.2, the pictorial warnings that must adorn duty-paid tobacco in Jersey follow EU legislation. This eliminates all non-EU nations (or other nations that have adopted the EU labelling standards) as potential sources of parallel imports.

However, the packaging requirements applied by the European Commission do not ultimately result in complete uniformity of packaging across the EU. The EU has a total of 24 official languages and while tobacco packaging must include warnings in the same size and format and using the same approved texts, the approved texts are displayed in the appropriate local languages of each member state. For example, tobacco packaging in Belgium carries warning messages and text imbedded in the pictorial warnings in Dutch, French and German. Similarly, packaging in Luxembourg carries warnings in French and German.

The pictorial warnings specified in the Packaging Regulations contain text (in English) embedded in the image. The presence of English text further reduces the pool of potential sources of parallel imported tobacco products to EU countries that use English in its warning messages. Three EU countries have been identified in which tobacco products are sold with warning messages in English: the UK, Ireland and Malta.

The Irish and Maltese picture warnings contain the prescribed pictures and text in English. However, they also contain similar text in Irish and Maltese that make the picture messages inconsistent with the picture messages required under the Labelling Regulations. Of these countries, only the United Kingdom has picture labels that are solely printed in English, consistent with the picture warnings required in Jersey.

The pictorial warnings required by the Packaging Regulations are a subset of the pictorial warnings that may be displayed on tobacco products destined for the UK market. Tobacco destined for the UK market is packaged with the same health warnings as tobacco destined for the Jersey market, except that UK tobacco packages carry an additional thirty pictorial warnings to the fifteen pictorial warnings listed in by the Packaging Regulations. The UK pictorial warnings carry fifteen different messages embedded into the picture: each message is imbedded in three different pictures, resulting in forty-five unique pictorial warnings.

Therefore, the only material difference between Jersey tobacco packaging and UK tobacco packaging is the presence of the UK fiscal mark<sup>23</sup>.

For some dutiable products, it is possible to obtain a refund of UK duty when goods are exported. For example, HMRC provides refunds on returned alcohol duty stamps that have been applied to bottles of spirits. These duty stamps are in sticker form; having the stickers returned allows HMRC to maintain control over the issue of stamps, and removes the possibility that the product in question could legally be returned to the UK market, since this would require the importer once again to affix a duty sticker.

However, HMRC does not offer refunds on tobacco products that bear the fiscal mark, unless they have been destroyed under HMRC supervision or repackaged<sup>24</sup>. The fiscal mark is printed on the package and unable to be removed without damaging the package. In addition, breaking the cellophane wrapper to replace the fiscal mark would affect product probity. Moreover, UK law stipulates that manufacturers must not apply the UK fiscal mark to tobacco products if those products are not required to carry a fiscal mark (e.g. where they are to be exported from the UK)<sup>25</sup>.

Therefore, if UK tobacco duty cannot be reclaimed from tobacco products for sale in the UK, it will be uneconomic for those products to be exported to the Channel Islands.

## 4.2. Exclusive import agreements

Virtually all tobacco products consumed in the duty-paid market in Jersey are imported by either JJ Fox or Longueville, under exclusive supply agreements that these companies have with the three largest tobacco manufacturers.

An exclusive distribution model is a very common form of distribution and there are many examples in Jersey of exclusive distribution agreements, in which a supplier agrees to sell its products to only one distributor for resale. Exclusive distribution can often lead to efficiencies where investments are needed to build or protect a brand image, most notably for new or complex products.<sup>26</sup> However, some of the anti-competitive risks associated with exclusive distribution are that intra-brand competition is reduced and markets are partitioned. Such agreements can have the effect of raising

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<sup>23</sup> This is a panel with the words "UK Duty Paid" printed on tobacco packets by the manufacturer before cellophane wrapping is applied. It confirms that UK duty has been paid on the tobacco by the manufacturer.

<sup>24</sup> Regulation 26 of the Tobacco Products Regulations 2001

<sup>25</sup> Regulation 23(3) of the Tobacco Products Regulations 2001 and section 8E of the Tobacco Products Duty Act 1979

<sup>26</sup> EC Guidelines on Vertical Agreements, paragraph 164

wholesale prices and depriving consumers of choice.<sup>27</sup>

Exclusive distribution agreements may infringe Article 8 of the *Competition (Jersey) Law 2005* if intra-brand competition is restricted or prohibited. The presence of exclusive supply provisions is likely to prohibit intra-brand competition. This increases the potential for consumer harm because it becomes difficult for new importers to enter the market and offer competition to the established importers in respect of their brands.

The assessment of whether this situation has the effect of hindering competition in the relevant market (and therefore infringes the Competition Law) requires a comparison of, on the one hand, the actual or likely future situation on the relevant market with the contractual restraints in place, and on the other hand, the situation that would prevail in the absence of the restraints. The JCRA has received evidence from a number of the tobacco manufacturers, stating categorically that they would only deal with a single importer to the Channel Islands, even in the absence of an exclusivity provision. The desire to deal with a single importer is apparently explained by the logistics of conducting the very small production runs for Channel Islands tobacco packets – the relevant manufacturers want to receive orders from a single source, and to have one company liable for taking the specially-produced stock.

On balance, then, we are unconvinced that exclusivity would change if the exclusivity provisions were set aside. On that basis, the JCRA does not intend to subject these provisions to further examination under the Competition Law. However, it remains the case that these exclusive agreements do have an effect on markets for tobacco products – in particular, in their consequences for retailer behaviour.

### **4.3. Restrictions on competition at retail level**

Competition at a retail level is also impaired by the structure of the market upstream.

The higher retailer margins in the Channel Islands compared to the UK would tend to indicate that competition between retailers of tobacco products in Jersey is less vigorous than is the case in the UK. Moreover, while we have not compiled recent retail price data as part of this market study, a brief observation of retail prices for individual brands at various outlets would seem to show that prices lie in a very narrow band, with no more than 5 or 10 pence difference for packets of 20 now costing in the region of £7. Certainly, the range of difference in prices for many individual grocery items observed during our groceries market study data collection late last year appeared to be considerably larger, both in absolute and percentage terms.

There may be a series of legitimate reasons why retailers are reluctant to compete vigorously in the sale of tobacco products. There are legal restrictions on advertising and promotional activities for tobacco products, although we understand that the rules on promotions in Jersey are currently less stringent than in the UK. Some retailers that we spoke to also indicated concern regarding the public perception of engaging in promotion of cigarette sales or being seen to compete keenly on price.

We have been told by the importers that, with rare exceptions, they sell their individual products to retailers at a common price. By contrast, in the UK, the terms at which the manufacturers sell their products to each customer are not universal and open to negotiation. As with other grocery categories, large retailers in the UK have buyers dedicated to the purchase of tobacco, and we are told that discounts, rebates, modifiers, incentive payments and over-riders are common. This ability for retailers to negotiate terms with the manufacturer encourages innovation on a contractual and

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<sup>27</sup> Ibid, paragraph 154

relationship level and fosters competition to a degree that cannot be achieved in a market in which each manufacturer has a single purchaser, and stock is sold at a single wholesale price. In addition, the fact that retailers can be aware of the prices at which their rivals procure products would be expected to lead to a less dynamic market, with the possibility of tacit co-ordination arising.

In our view, allowing Jersey retailers to purchase tobacco directly from manufacturers or wholesalers outside the Channel Islands would lead to a reduction in the retail price of tobacco products in Jersey, in part because the importers would be subject to competition, but also because larger retailers would be able to leverage their existing buying functions, as well as their distribution networks in transporting tobacco products to their stores, with less duplication of assets and expertise. In turn, an increase in competition in the downstream markets could ignite greater competitive pressure in the retail market as retailers would be able to shop around and would be more conscious of the prices they are paying and therefore their ability to undercut competitors.

The features of the market outlined in sections 4.1 and 4.2 – that is, the inability to engage in parallel trade and the existence of exclusive import agreements – mean that retailers are currently unable to purchase directly from manufacturers. In our view, encouraging parallel trade and allowing retailers to source tobacco products outside the Channel Islands is the clearest means of increasing competition in these markets and reducing the extent of the difference in pre-tax prices between the UK and Jersey. Possible means of facilitating parallel trade are explored in section 5.

## 5. Potential remedies

In section 4, the absence of the ability to engage in parallel trade was identified as a key barrier to Channel Islands' retailers and consumers accessing tobacco products from other, more competitive markets, where pre-tax prices are lower. This section of the report focuses on two potential remedies to facilitate parallel trade:

- a. Establishing an agreement with other territories regarding common packaging, thereby enabling importers and retailers to source tobacco products from those other territories, rather than being required to stock only Channel Islands packets; and
- b. Establishing a customs agreement with the UK and Isle of Man (possibly together with Guernsey), under which tobacco duty revenues would be pooled and shared, and tobacco products bearing the "UK Duty Paid" mark could be sold in Jersey.

Also explored in this section is the concern expressed that importers and/or retailers are engaging in "profiteering" at the time of duty increases. In the JCRA's view, the most straightforward solution would be the development of bonded warehouses with anti-avoidance rules similar to those already applied by HMRC in the UK.

### 5.1. Agreement with other territories for common packaging

One option for the States of Jersey in facilitating parallel trade in tobacco products would be to seek agreement on common packaging and health warnings with other territories that do not use fiscal marks.

As discussed in section 4, a combination of health labelling requirements and fiscal integrity measures in both Jersey and other jurisdictions means that the only cigarettes that can currently be sold in the duty-paid market in Jersey are those manufactured specifically for sale in the Channel Islands. Jersey does not apply a fiscal mark itself, but legislation does require the use of particular pictorial health warnings, of the type now prescribed in the EU (see Appendix 4 and footnote 8, above). The warnings must also appear in English, to ensure that they are easily understood by consumers in Jersey.

The JCRA understands that use of pictorial health warnings is common to most tobacco packaging in territories within the EU. However, because health warnings are typically in the local language of the relevant state (to ensure the effectiveness of the warning), it would not be possible to import to Jersey tobacco products which have been manufactured for sale in a territory that does not have English as its main language.

Of the territories within Europe that have English as their main language, both the UK (together with the Isle of Man) and the Republic of Ireland apply fiscal marks in a manner that would render it impossible to import them to Jersey without the imposition of duties in that other state.

However, it is noteworthy that the English-speaking territory of Gibraltar, like Jersey (and Guernsey) does not apply a fiscal mark to tobacco products sold in the duty-paid market there, although it does require a health warning in English on the packet. Some tobacco products sold in the duty-paid market in Gibraltar are in fact labelled as being for duty-free sale only. We understand that given the small size of the territory and the relatively low duty rate, the customs authorities in Gibraltar will allow such sales, in part to increase the range of brands available for sale. We have explored with JCIS whether a similar approach could be adopted in Jersey. However, JCIS has identified that

the adoption of a similar policy would greatly complicate their efforts to control smuggling, since they would be unable to differentiate between tobacco products on which Jersey tobacco duty had been paid, and products which had been purchased in the duty-free market and were being re-sold.

While some tobacco products sold in Gibraltar are in duty-free packaging, other brands (e.g. Silk Cut) are sold in packaging in English with health warnings (although not pictorial health warnings). To the extent that these packets are produced specifically for the Gibraltar market, their production faces similar small scale issues to those described by manufacturers of the Channel Islands packets<sup>28</sup>. However, both the pre-tax and post-tax retail prices of cigarettes in Gibraltar are substantially lower than in Jersey.

The retail price of a packet of 20 cigarettes in Gibraltar in September 2013 was £2.36 (Marlboro) and £2.39 (Silk Cut) – both of these brands are included in the ‘netback’ analysis of Jersey cigarette prices in section 3 above. Of this retail price, £1.10 was Gibraltar tobacco duty, which leaves a pre-tax price of £1.26 and £1.29. By contrast, based on the netback analysis for the period April 2012-March 2013, the average pre-tax price of a packet of 20 cigarettes in Jersey was £2.51 (almost double the figure in Gibraltar), made up of £1.30 manufacturer price, 37p importer margin and 84p retailer margin.

At present, tobacco products produced for sale in Gibraltar cannot be sold in the duty-paid market in Jersey because they do not carry the requisite pictorial health warnings. If it were possible for Jersey retailers to source cigarettes from Gibraltar (or from wholesalers who sell to retailers in Gibraltar), then the pre-tax price of cigarettes in Jersey could be expected to fall sharply, although the retail price actually paid by consumers in the duty-paid market would still ultimately depend predominantly on the level of tobacco duties set by the States of Jersey.

One option for the States of Jersey in facilitating parallel trade in tobacco products would therefore be to seek agreements regarding uniformity of packaging and health warnings with other English-speaking territories in Europe, such as Gibraltar, which do not use fiscal marks. This would increase the pool of potential wholesale suppliers, and increase the size of the production runs, thereby potentially decreasing the unit manufacturing cost. In this context, it is interesting to note the recent adoption of a new Tobacco Directive by the EU<sup>29</sup>, which is expected to come into force next month and will require all Member States<sup>30</sup> to ensure that pictorial warnings appear on all cigarette packaging by May 2016. In light of the fact that it appears that Gibraltar will need to consider amendments to its tobacco packaging legislation over the next two years, there might be an opportunity for representatives from Jersey to seek discussions in coming months regarding uniformity of packaging requirements, based on the Packaging Regulations.

In response to the possibility of sourcing tobacco products from wholesalers in other jurisdictions, an existing importer of tobacco products to Jersey noted that it considers it best practice to secure indemnities on product liability from manufacturers, and that to do otherwise would “expose the company to catastrophic litigation at the hands of third parties”. If parallel trade in tobacco products were able to be facilitated (whether by agreement with other jurisdictions on packaging or a duty-sharing agreement with the UK – see below), then clearly it would be up to wholesalers and retailers in the Channel Islands to consider what contractual indemnities to seek with respect to their procurement and sale of these products. While it is recognised that the potential exposure to liabilities in relation to the sale of tobacco products is unusual when compared to most other goods, the fact that an existing importer chooses to seek these indemnities does not, of itself, mean that parallel trade into Jersey via parties other than manufacturers would be unfeasible or impractical.

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<sup>28</sup> While the population of Gibraltar is less than half that of Jersey, the volume of tobacco products sold per capita is reported to be significantly larger.

<sup>29</sup> See footnote 8

<sup>30</sup> While Gibraltar is part of the EU, it is outside the Customs Union and VAT area



## 5.2. Duty-sharing agreement with the UK

Another method of facilitating parallel imports of tobacco products would be to enter a duty-sharing agreement with UK with respect to tobacco duties.

There is a precedent for such an agreement in the form of Common Purse Agreement (**the CPA**) between the UK and the Isle of Man, which sets up a customs union between the two entities and entitles the Isle of Man to a share in the United Kingdom's Customs and Excise revenues. As the UK is a member of the EU, the Isle of Man is effectively in a customs union with the entire EU.

The CPA sets up a 'common purse' for the receipt of duties and revenue, which is then split between both treasuries according to agreed formulas. Tobacco duties are shared based on the "fiscal population" of the two jurisdictions. The fiscal population is calculated by adjusting the actual population to take account of visitors to the Isle of Man. No account is made of visitors to the United Kingdom. Each visitor to the Isle of Man adds approximately 0.18 of a head to the fiscal population count.

As a result, tobacco products can be sold in the Isle of Man bearing the "UK Duty Paid" panel. We understand that large retailers in the Isle of Man use their UK procurement and distribution networks to source tobacco products directly from UK manufacturers, and that the pre-tax and post-tax prices of cigarettes in the Isle of Man are very similar to those in the UK (due to the CPA, the taxes and duties in the two jurisdictions are the same).

It would be possible, at least in theory, for a similar division of tobacco duty revenues to occur between Jersey (and Guernsey) and the UK, based on a fiscal population. Alternately, given that virtually all tobacco products imported into Jersey are either manufactured in the UK or transit the UK on their journey to Jersey, it would be possible for HMRC to collect duty in the UK before onward export to the Channel Islands, and then for the three customs authorities to monitor the volumes of tobacco products flowing between the jurisdictions (as they do presently). Duty revenues could be apportioned on a regular basis using the flow data to identify the jurisdiction in which the product was likely to have been consumed.

Entering into a duty-sharing agreement with the UK would undoubtedly lead to the parallel importation of tobacco from the UK and would ultimately be expected to lower pre-tax Jersey tobacco prices towards those observed in the UK while simultaneously increasing the post-tax price of tobacco, increasing revenue generated for the Treasury by tobacco products.

However, while this solution has theoretical appeal, it has a number of potential drawbacks:

- As outlined above in section 2.1.3, the methods for calculating duty liability on tobacco products, and the actual duty rates, differ significantly between Jersey and the UK. For example, the analysis conducted as part of this market study found that duty charged on an average pack of 20 cigarettes in Jersey over the 12 months from April 2012 to March 2013 was approximately £3.58. In the UK, the value of the duty charged on the same average pack of cigarettes amounted to approximately £4.36. In this instance, adopting a common purse agreement with the UK for tobacco duty would presumably entail Jersey not only changing the manner in which duty liability on tobacco products was calculated (adopting the UK and Isle of Man duty structure of duties, as well as the timing of duty increase – see section 2.1.3 above), but also increasing the duty charged on tobacco products to UK levels – otherwise, there would be an arbitrage opportunity between Jersey and UK, putting UK tobacco duty revenues at risk. Whether the requisite significant increase in tobacco duty is appropriate would be a matter for the States of Jersey.

- While an agreement could lead to more efficient collection of tobacco duties, the potential gains (in the form of reduced pre-tax prices and increased revenues for the Treasury) would almost all accrue to Jersey, rather than the UK, so it is hard to see the basis for HMRC agreeing to take on this added responsibility, especially if it only related to tobacco duties. By contrast, the Isle of Man CPA is wide-ranging and covers all indirect taxation (including VAT).
- Such an agreement would also imply that Jersey would have to adopt UK regulations on tobacco packaging, which could entail a loss of sovereignty for Jersey. For example, if the UK were to adopt plain packaging, the same reform would have to apply in Jersey as well under a customs agreement of this type.

Whether such an agreement is feasible in the face of such drawbacks, and whether the benefits outweigh the costs (e.g. loss of sovereignty), is a matter for the States to consider.

### **5.3. “Profiteering” and bonded warehouses**

It has been suggested that parties involved in the tobacco supply chain have engaged in ‘profiteering’; in particular, by increasing the price of cigarettes on the date the duty increase is imposed despite stock having been imported and duty paid prior to the duty increase.

On 1 January 2013, the rate of duty on cigarettes in Jersey increased by 13.2%. At that time, all duties were collected by JCIS at the point of import, so the higher rate only began to apply to products that were imported after that date. However, it was widely reported in the local media that the price of cigarettes in retail outlets rose sharply on or about 1 January (and, it was said, in some cases prior to 1 January), despite the fact that the stock being sold at that higher price would have been imported some weeks or months before, and would have attracted the preceding, lower rate of duty. It was suggested that this was evidence of parties involved in the tobacco supply chain in Jersey engaging in “profiteering”.

There were conflicting accounts from importers and retailers as to the point at which the wholesale price of cigarette stocks increased, so it was unclear whether multiple levels of the supply chain were implicated. As observed in section 3, of all of the levels of the supply chain for tobacco products in Jersey, retailing is the one which features a significant number of potential competitors. Indeed, given that cigarettes are frequently bought as a one-off purchase, rather than as part of a “weekly shop”, there are arguably far more outlets competing directly (supermarkets, convenience stores, petrol forecourts) than would be the case for other types of groceries.

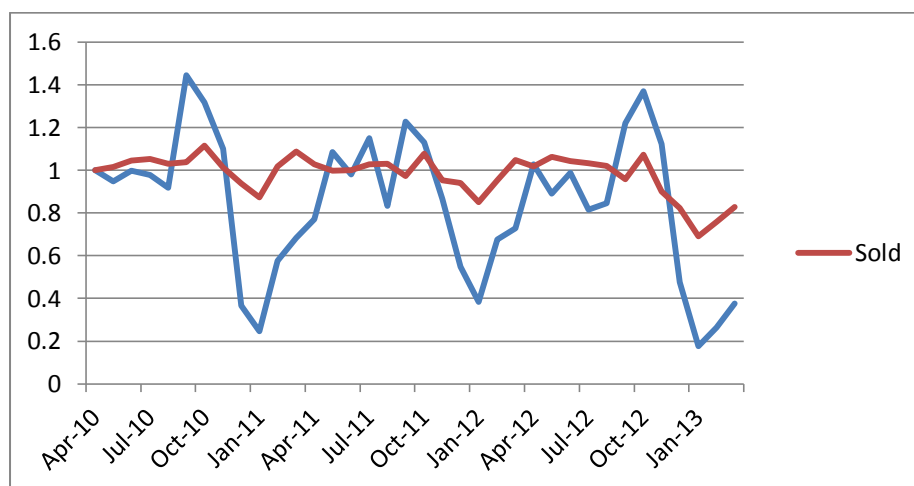
As private commercial businesses, the retailers’ aim will, of course, be to maximise the margin between the price at which they purchase goods and the price at which those goods are sold to customers. Competition law does not intrude in price-setting decisions, provided that the firm is not dominant (which would clearly not be the case with respect to tobacco retailing in Jersey) and that prices are not being set as part of an agreement between firms (e.g. a price-fixing cartel). The evidence that we collected showed that the timing of the increase in the retail price varied between different shops, and that at least two major chains did not increase their cigarette prices until several weeks after New Year. While this does not establish categorically the absence of a cartel, it does suggest that an agreement is less likely to be in place.

It is possible that many retailers simply anticipated that, as in past years, much of the ‘market’ would put through a price increase reflecting the duty increase as soon as possible after New Year, and that consumers either would have expected such an increase to occur or were unlikely to shop around for cigarettes. This behaviour could best be described as ‘tacit collusion’ – where no agreement

exists between suppliers, but the circumstances of the market allow suppliers to have expectations about the conduct of other suppliers. Certainly, the fact that many retailers were able, on a temporary basis, to increase substantially the margins that they earn on tobacco products is, at the very least, consistent with our finding that competition between retailers in the supply of tobacco is not especially vigorous. Those retailers who increased margins in this manner clearly did not consider that they were taking a material risk of being undercut by others or of losing business by consumers ‘shopping around’. For the reasons outlined in sections 3 and 4, our judgment is that the best means of increasing competition between retailers for these products is to allow parallel trade, so that retailers are obtaining stocks from a range of suppliers at a range of wholesale prices, rather than, as at present, purchasing from one supplier at a uniform wholesale price. This would allow certain retailers to gain a competitive advantage through procurement and increase ‘uncertainty’ for those retailers.

In terms of the timing of the duty rise changing firms’ behaviour, it is indisputable, based on the evidence that we have reviewed, that there is a spike in imports in the months before year end and a sharp drop after the new rate of duty takes effect. Tobacco is durable enough that it can be stockpiled for a period of time. The JCRA understands that tobacco is generally considered to have a shelf life of between six and twelve months before the quality of the product has degraded to the point that customers may notice the change in quality. In the absence of measures restricting the volume of tobacco an importer may purchase in the lead up to any increases in duty rates, the lag between the announcement of new duty rates and their application allows importers to stockpile product in advance of the duty increase and then sell this product at a higher price once the duty increase has come in to force.

**Figure 5: quarterly imports and sales by Jersey importers, 2010-2013**



The data we have collected as part of this study indicates that this is a practice that has been routinely engaged in by the importers, reflecting, perhaps, the fact that the States of Jersey has significantly increased the duty rates levied on tobacco products over recent years. Figure 5 above illustrates the volume of the top 20 selling cigarette varieties imported by the Jersey importers from manufacturers and the volumes of the same varieties sold by the Jersey importers to Jersey retailers, quoted on a quarterly basis. The data has been indexed to protect the confidentiality of the data, with the volumes bought/sold in April 2010 being the base of 1. For both imports and sales, there are clear spikes in volumes in the last quarter of the year, followed by clear troughs in the first quarter of the following year. However, the peaks and troughs in the volumes imported are much more pronounced than those for the volumes sold, and only a small proportion of the volumes imported can be explained by demand.

It is arguable that any commercial business would seek to secure inputs when they are cheaper, especially if a significant price increase is pre-announced, or, at the very least, a likely prospect. This conduct is also observable in other, far more competitive markets (e.g. the UK). However, it is recognised that it can produce material reductions in duty revenues for the Treasury.

The most straightforward remedy to this phenomenon would be to facilitate the introduction of bonded warehouses for the tobacco importers. A bonded warehouse is a building or other secured area in which, in this case, tobacco may be stored without the payment of duty, even after having been imported. Upon entry of goods into the warehouse, the importer and warehouse proprietor incur liability under a bond. This liability is generally cancelled when the goods are:

- destroyed under JCIS supervision; or
- withdrawn for consumption domestically, and there has been payment of the duty liable on the goods withdrawn.

A bonded warehouse allows importers more control over the payment of duty because the importer can withdraw goods from the warehouse as demand dictates and it is only when goods are withdrawn that a liability for duty arises. In the absence of a bonded warehouse, an importer is liable for duty as soon as the boat carrying tobacco docks in the harbour.

The JCIS has, in the past 12 months, reached agreement with both main importers of tobacco to Jersey to establish bonded warehouses.

However, in order to ensure that the owner of a bonded warehouse does not simply move all stock out of bond (i.e. from one end of the warehouse to the other) on the day before a duty increase takes place, it would be advisable to have anti-forestalling arrangements in place, under which the amount of stock that can be moved out of bond in the period before a duty rate change is restricted (essentially, by reference to “normal” levels of stock movement). HMRC has implemented such arrangements in the UK<sup>31</sup>, and we believe that it should be possible for JCIS to take similar action under its own bond arrangements with importers.

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<sup>31</sup> HMRC, *Anti-forestalling restrictions: cigarettes, Notice 85C* (December 2009)

## Appendix 1- Terms of reference

**Request by the Minister for Economic Development for the Jersey Competition Regulatory Authority (JCRA) to produce a report examining the market for the supply of cigarettes and hand-rolling tobacco in Jersey under the authority of Article 6(4) of the Competition Regulatory Authority (Jersey) Law 2001.**

In light of the current public interest surrounding the cost and pricing of tobacco products locally, I have decided to request the JCRA to undertake a study into the market for the supply of cigarettes and hand-rolling tobacco in Jersey, in the terms detailed below. As this is a request under Article 6(4) of the Competition Regulatory Authority (Jersey) Law 2001, it provides the JCRA with powers under Article 26(2) of the Competition (Jersey) Law 2005 to require the provision of information, etc.

The aims of the review should be as follows:

1. To undertake an analysis of prices, costs and profits at the importation, wholesale and retail levels of the supply of cigarettes and hand-rolling tobacco in Jersey;
2. To produce a report on the level of competition in the supply of cigarettes and hand-rolling tobacco in Jersey, with specific reference to exclusive agreements, making any such recommendations for changes or improvements that might be considered.

The scope of the review should cover cigarettes and hand-rolling tobacco. In particular, it is requested that the report:

1. Compares the average wholesale and retail prices for cigarettes and hand-rolling tobacco sold in Jersey with prices charged in the United Kingdom and any other relevant jurisdictions based on available data;
2. Gives consideration to regulations in respect of the import and supply of cigarettes and hand-rolling tobacco in Jersey, as well as the States of Jersey Tobacco Strategy, and whether they impact on competition;
3. Considers and reports on any other relevant matters that may arise during the course of the JCRA's review.

## Appendix 2- States of Jersey Tobacco Control Strategy (2010-2015)

### A Tobacco Strategy for Jersey 2010 - 2015

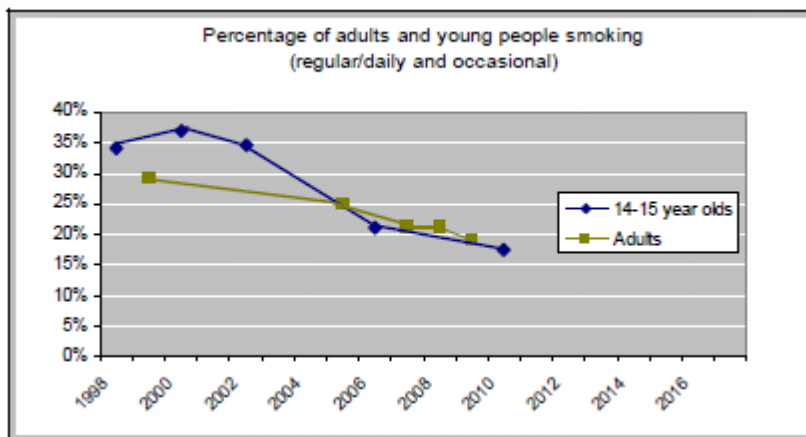
Our vision is of a smokefree future. It is a future, where our Island is free from the harms of tobacco use and where islanders lead long healthy lives. A future free from tobacco use will mean our children will not have their lives shortened unnecessarily from smoking-related illnesses.

There has been a fall in the number of people who smoke in Jersey. The existing tobacco strategy has been very successful to date, seeing smoking prevalence decrease from 29% to 19% for adults and from 35% to 17% for 14-15 year olds during the last seven years. The cumulative and coordinated efforts have helped save many lives. The key lesson learned is that by joining legislative, fiscal and educational initiatives together we can make a difference to public health.

Over the last decade, a similar reduction in prevalence has been achieved in England with reductions from 28% to 22% in smoking. The current annual cost saving from the reduction in smoking prevalence is estimated to be £380 million <sup>1</sup>.

Figure 1: Percentage of adults and young people smoking

Figure 1: Percentage of adults and young people smoking

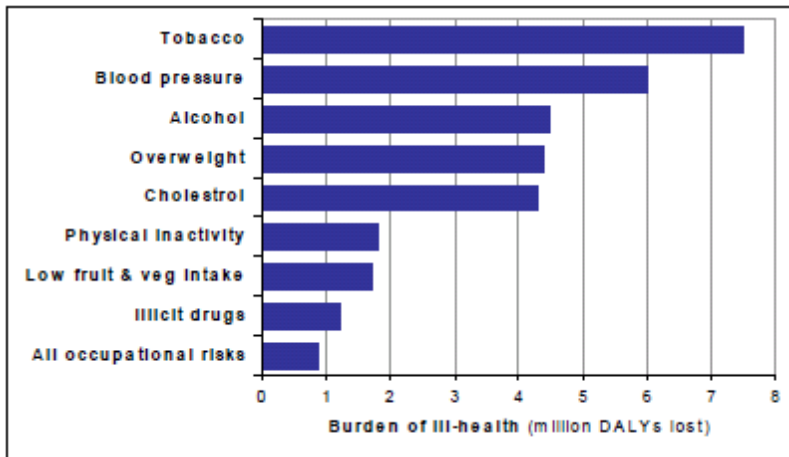


Source (Public Health Intelligence Unit)

### Maintaining Momentum

This is not a time to rest on our laurels. Most smokers start young and once addicted people often need specialist help to stop. Smoking kills half of all long-term users and remains the biggest preventable cause of premature death in Jersey <sup>2</sup>(figure 2). Locally, every year an estimated 355 years of life are lost prematurely due to cancers of respiratory organs - mostly the lung - which are closely related to tobacco use.

Figure 2 Burden of ill health (Disability Adjusted Life Year's)



Source: European Commission.

### Health & Consumer Protection

Protecting children's health is a high priority for everyone. Hospital data indicates around 400 babies are discharged home from the maternity ward each year to a household where at least one person smokes. The harmful effects of passive smoking for children include: cot death, meningitis, asthma and glue ear. A careful review of the evidence and greater clarity of potential benefits for extending existing smoke free regulations need to be completed.

Smoking also has a cost to local industry. This cost is often hidden, in terms of reduced productivity of workers, increased sickness and absenteeism, cleaning and maintenance. A fit and healthy workforce is good for the Island as a whole as it should give the island a competitive edge when attracting new business and investment.

The case for further action is clear. This strategy proposes three areas for action. They are;

1. Reduce the number of children and young people taking up smoking
2. Protect families and communities from tobacco related harm
3. Motivate and assist every smoker to quit

The actions under each priority are consistent with tobacco control policy in England and the European Convention of Tobacco Control. Due to previous successes in reducing the number of smokers in Jersey, this strategy sets new and challenging targets for lowering the number of adults and children who smoke. Meeting these targets will help realise the vision of a smoke free Jersey, which will enable us all to live longer and healthier lives.

#### Objective 1: Prevent children taking up smoking

Children are most likely to take up smoking during their teenage years. It is estimated that someone who starts smoking at the age of 15 is three times more likely to die of smoking-related cancer, than someone who starts in their late 20s. In Jersey the number of young people who describe themselves as 'smoking regularly', doubles between the ages of 13 and 16 years of age. There are more young girls who take up smoking during their adolescent years than boys.

## Proposed Action:

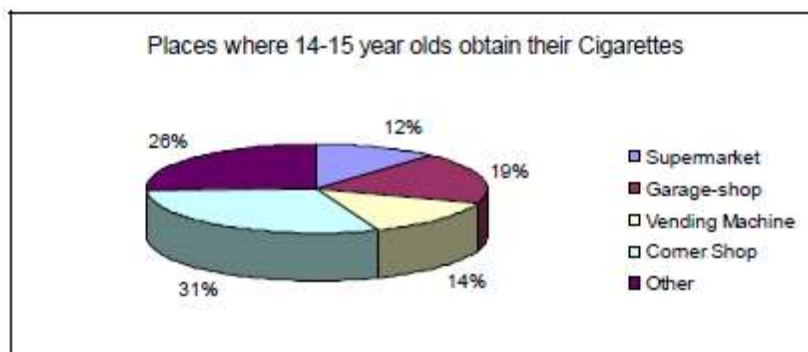
1. To reduce the affordability of tobacco: Economic models show that a 10% increase in price leads to a 2% drop in smoking prevalence across the population <sup>3</sup>. There is considerable evidence to show that making tobacco less affordable is an effective way of reducing the prevalence of smoking, particularly for children and young people.

- Agree with the Treasury and Resources Department an appropriate tax escalator which would last for the period of the strategy.
- Explore the implications for Jersey of the European Union decision to implement tax harmonization on tobacco products in 2011

2. To reduce the availability of tobacco: Children acquire tobacco from a number of different sources. Local surveys show that garages, corner shops and vending machines are the most frequent sources of tobacco for children. Other sources may include family members.

- Prohibit the sale of tobacco by vending machines
- Examine different approaches to reducing underage sales
- Explore the impact of duty-free sales on under-age smoking
- Prohibit tobacco advertising at point of sale

Figure 3: Places where 14-15 year olds obtain their Cigarettes



Source (Public Health Intelligence Unit)

3. Increase awareness of the harm caused by Tobacco. When communicating to young people we need to consider the potential for new technology and media to create new methods of passing on information about the harm of taking up smoking and the benefits of a smoke free future. This includes differentiating between messages that target boys and girls.

- Implement social marketing approaches that target young people
- Support peer education approaches to delivering key messages about tobacco

## Objective 2: Protect Families and Communities from Tobacco related harm

Smoking is now no longer the norm. The implementation of smoke free legislation means that virtually all workplaces and public places are free of the hazard of second hand smoke. There is emerging evidence of the harmful effect of second hand smoke in other confined spaces such as cars and homes.



Proposed Action:

Consideration needs to be given to the benefits of extending existing smoke free legislation. In order to achieve this we need to;

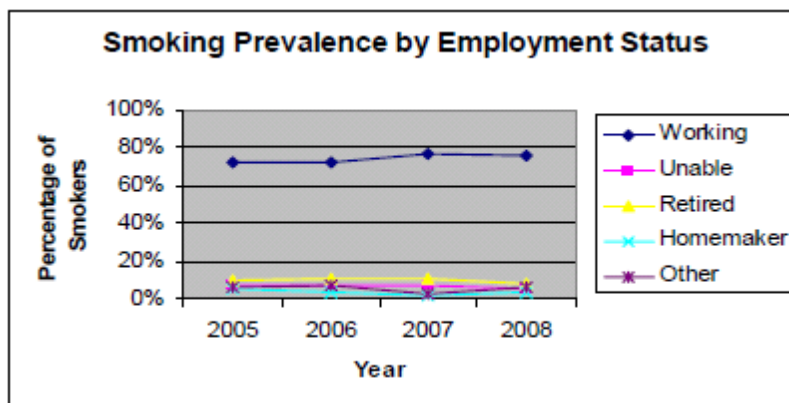
- Assess and review the evidence for extending smoke free legislation to other public spaces
- Assess and review the evidence for extending smoke free legislation to all motor vehicles'
- Work with community groups to help people make their homes, cars and play spaces smoke free
- Work with Transport and Technical services to reduce the unwanted effects of tobacco related litter

Objective 3: Motivating and assisting every smoker to quit

Getting the right information at the right time at the right place is the key to helping people to quit. Just over a thousand smokers contacted the service during 2009. Demand for the service remains high with waiting lists during busy parts of the year. On average twenty stop smoking clinics are run each week with between 12 - 16 people seen in each clinic.

Locally, the majority of smokers are working, a smaller yet consistent number of smokers describe themselves as retired, homemakers or unable to work. The challenge for the service is to ensure it is accessible and easy to use in the different contexts of smoker's everyday lives.

Figure 4: Smoking Prevalence by Employment Status



Source (Public Health Intelligence Unit)

Proposed Action:

Expand the reach of the Help 2 Quit service without compromising its quality and success rate. In order to achieve this we need to:

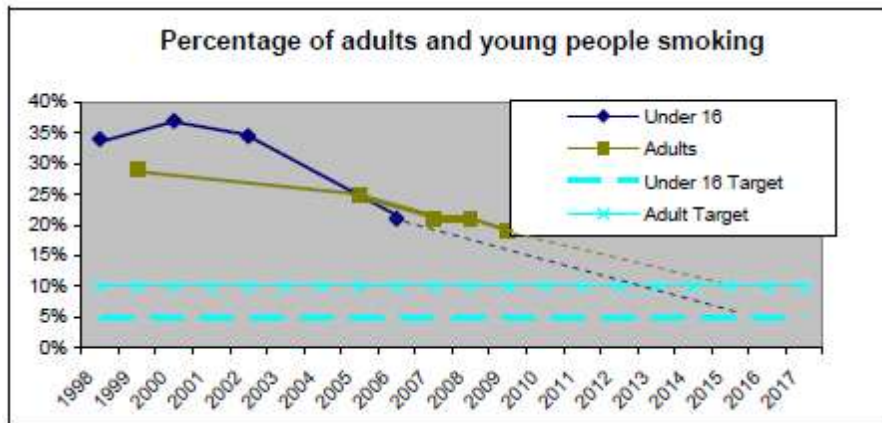
- Develop service level agreements with general practice and community pharmacists to extend the reach of the cessation service
- Explore opportunities for public private partnership to deliver smoking cessation in the workplace
- Develop and implement a marketing strategy to promote the smoking cessation service

- Develop targeted cessation services for key groups such as pregnant women, ethnic minorities, mental health service users and prisoners

### Key Measures for Success

#### Five year Headline target

- Reduce the prevalence of smoking in adults to 10%
- Reduce the prevalence of children under 16 years old who smoke to under 5%



Source (Public Health Intelligence Unit)

#### Five year indicators for success

- Increase the proportion of smokers contacting cessation services from 7% to 20%
- Increase the number of smoke free homes to which babies are being discharged.
- Extend the reach of all Help 2 Quit to key target groups
- Reduce to nil the number of under aged purchases as reported in the child health survey

### Strategy Delivery

The Public Health Department will lead the implementation of the actions outlined in this strategy. The formation of a tobacco alliance will serve as a way of engaging key States Departments and other stakeholders to secure success.

<sup>1</sup> Action on Smoking and Health:(2009): Beyond Smoking Kills, protecting children and reducing inequalities: Action on Smoking and Health

<sup>2</sup> Alcohol Related harm in Europe - Key data. Factsheet. October 2006. European Commission, Health & Consumer Protection, Directorate-General.

<sup>3</sup> Jha P, Chaloupka FJ: (2009) Curbing the Epidemic: Governments and the Economics of Tobacco Control. World Bank.

## Appendix 3- Data Requests

The JCRA collected price, and volume data from entities engaged in each step of the supply chain.

### *Manufacturers*

Manufacturers were asked to provide the following data covering the period April 2010 to March 2013 for their ten top-selling cigarette products and top two rolling tobacco products in Jersey:<sup>32</sup>

- Average sale price per packet (Jersey and Guernsey)
- Average sale price per packet to selected retailers (UK)
- Recommended Retail Price
- Weight of Cigarette/rolling tobacco for purpose of duty calculation
- Monthly volume delivered to Jersey importer of each of the top 10/2 selling products for period April 2010 to March 2013

PMI refused to provide data relating to the UK market, but did provide data for the Channel Islands markets.

### *Channel Island Importers*

For their ten top-selling cigarette and two top-selling rolling tobacco products in Jersey, importers were requested to provide:

- Average annual purchase price per product from manufacturer (excluding duty and GST) for the period 2010 to 2013 (Jersey and Guernsey)
- Average annual purchase sale per product to retailers (excluding duty and GST) for the period 2010 to 2013 (Jersey and Guernsey)
- Value of duty paid for each product for each year for the period 2010 to 2013 (Jersey and Guernsey)
- Monthly volume of each 10/2 products delivered by manufacturer for period April 2010 to March 2013
- Monthly volume sold of each 10/2 products sold to retailers for the period April 2010 to March 2013
- Number of regular customers in Jersey (regular is supplied at least monthly)
- Top five customers and value of their custom for the period April 2012 to March 2013
- Management Accounts

### *Retailers*

Retailers were asked to provide:

- Average purchase price paid by (Jersey/Guernsey/UK) business (excluding GST/VAT, duty,

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<sup>32</sup> Data for the same 12 products were also collected for the UK and Guernsey.

overrides and discounts) for the period April 2012 to March 2013.

- Average sale price in Jersey/Guernsey/UK (excluding GST/VAT and duty).
- Monthly sales volumes for the 10/2 tobacco products for the period April 2012 to March 2013.

Data was not always provided in format requested, particularly the retail prices, which were provided including GST/VAT and duty.

### *Cross-Checking Data*

There are two primary sources of the data used to calculate the manufacturers and importers margins. The manufacturers' margin, which is defined at the price manufacturers receive for a product, can be calculated by using the price importers have stated that they pay the manufacturers for each tobacco product or it can be calculated using the price at which manufacturers state that they sell each tobacco product to the importers. The two prices should be exactly the same.

In some circumstances, the JCRA has not been able to cross-check the data provided by the importers because the corresponding data has not been provided by the manufacturers. In particular, PMI and JTI refused to provide the requested price information relating the UK market.

JTI did not provide reasons for refusing to provide the requested information.

PMI stated that it refused to provide the requested information on the UK market because its wholesale prices vary considerably from market to market and it considers the Channel Islands as a distinctly separate market from the mainland UK, referencing the different packaging requirements, duty and tax rates, size of the markets and the related manufacturing and logistics costs. PMI stated that based on those factors and its own commercial decisions, its profit margin may also vary between the market and the wholesale prices in Jersey are likely to be higher than in larger market such as the UK. For these reasons, PMI stated that it considered a comparison between Jersey and the UK to be unhelpful and likely to lead to misleading assumptions.

### *Duty-free*

As noted in Section 2.2.4, the JCRA has not attempted to calculate the value or volume of the duty-free tobacco market in Jersey. The JCRA did, however, contact the transport operators (air and sea) that account for the significant proportion of international passengers entering Jersey and collected data on the prices at which each operator purchases duty-free tobacco and the prices at which they sell the same products to retail customers on-board.

These operators were requested to provide:

- Average purchase prices of top ten selling cigarette and top two selling rolling tobacco items;
- Average sale prices for their top ten selling cigarette and top two selling hand rolling tobacco products; and
- Suppliers for whom they purchase their products.

## **Appendix 4 - Restriction on Smoking (Warning Notices) (Jersey) Regulations 2011**



## RESTRICTION ON SMOKING (WARNING NOTICES) (JERSEY) REGULATIONS 2011

### Arrangement

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Jersey

## RESTRICTION ON SMOKING (WARNING NOTICES) (JERSEY) REGULATIONS 2011

*Made*

*18th January 2011*

*Coming into force*

*25th January 2011*

**THE STATES**, in pursuance of Articles 1, 1G and 2 of the Restriction on Smoking (Jersey) Law 1973<sup>1</sup>, have made the following Regulations –

### 1 Interpretation

In these Regulations, unless the context otherwise requires –

“back”, in relation to a packet of tobacco, refers to the external surface opposite the front;

“EEA state” means any of the following –

- (a) a member State of the European Union;
- (b) a Contracting Party to the Agreement on the European Economic Area signed at Oporto on 2nd May 1992 as adjusted by the Protocol signed at Brussels on 17th March 1993;

“front”, in relation to a packet of tobacco, means the external surface of the packet which is, or is equal in area to, the largest surface and either –

- (a) faces a person opening that packet; or
- (b) where no surface faces a person opening the packet, carries most prominently the name, trademark or other distinguishing mark of the brand of tobacco;

“Law” means the Restriction on Smoking (Jersey) Law 1973<sup>2</sup>;

“packet”, in relation to tobacco, means any box, package, container, wrapping or other receptacle which contains the tobacco, and in which the tobacco is, or is intended to be, presented for retail supply, excluding any additional transparent outer wrapping which may be discarded on opening and excluding any wrapping of individual cigars or cigarillos, and where any receptacle is or is to be contained in another receptacle (excluding such outer wrapping), includes each such receptacle;



“picture warning notice” means the warning consisting of the photograph, illustration or other graphic under each heading in paragraphs 1 and 2 of Schedule 1;

“producer”, in relation to a packet of tobacco, means a person who in the course of a business –

- (a) manufactures it;
- (b) puts a name, trademark or other distinguishing mark on it, by which he or she holds himself out to be its manufacturer or originator; or
- (c) imports it into Jersey.

with a view to the tobacco that the packet contains being supplied for consumption in Jersey or through the travel retail sector, and “produce” shall be construed accordingly;

“tobacco for oral use” means any product made wholly or partly of tobacco which is –

- (a) intended for oral use, unless intended for smoking or chewing; and
- (b) either –
  - (i) in powder or particulate form or any combination of these forms, whether presented in sachet portions or porous sachets or in any other way, or
  - (ii) presented in a form resembling a food product;

“travel retail sector” means retail outlets in Jersey at which duty free packets of tobacco may be purchased only by people who are travelling on journeys to destinations outside Jersey.

## 2 Requirements for warning notices

- (1) A producer of packets of tobacco other than tobacco for oral use and smokeless tobacco shall ensure that each packet produced by him or her carries –
  - (a) on its front the following written warning notice –
    - (i) “Smoking kills”, or
    - (ii) “Smoking seriously harms you and others around you”; and
  - (b) on its back a picture warning notice from the list of picture warning notices in paragraph 1 of Schedule 1 or, where it applies, paragraph 2 of Schedule 1, printed in accordance with the technical specifications set out in paragraph 3 of that Schedule.
- (2) A producer of a packet of tobacco intended only for supply in the travel retail sector may use the picture warning notice in paragraph 2 of Schedule 1 instead of the picture warning notice set out in paragraph 1(14) of that Schedule.
- (3) A producer of a packet of a brand of tobacco other than tobacco for oral use and smokeless tobacco shall ensure that –
  - (a) the text of each notice set out in paragraph (1)(a) appears on between 47.5% and 52.5% of the total number of the packets of



- 
- tobacco of that brand that the producer produces over any period of 12 months; and
- (b) each picture warning notice described in paragraph (1)(b) appears on between 4.16% and 8.33% of the total number of the packets of tobacco of that brand that the producer produces over any period of 12 months.
- (4) In the case of packets of tobacco other than packets which immediately enclose the tobacco, the period for measuring the frequency of the picture warning notices as described in paragraph (3)(b) shall be 3 years instead of 12 months.
- (5) A producer of packets of smokeless tobacco shall ensure that each packet carries on its front the warning notice "This tobacco product can damage your health and is addictive".

### **3 Size of warnings**

- (1) A producer of a packet of tobacco shall ensure that, subject to paragraph (2), in relation to each packet of tobacco produced by him or her –
- (a) the text specified in Regulation 2(1)(a) or in Regulation 2(5) covers an area amounting to at least 30% of the front of the packet; and
- (b) the picture warning notice referred to in Regulation 2(1)(b) covers an area amounting to at least 40% of the back of the packet.
- (2) Where the front of the packet of a tobacco, other than the front of a packet of cigarettes, exceeds 75 cm<sup>2</sup>, the areas specified in paragraph (1) shall not apply and instead the text or picture warning notice, as the case requires, must each cover an area of at least 22.5 cm<sup>2</sup>.

### **4 Requirement for yield statement on packets of cigarettes**

- (1) A producer of a packet of cigarette shall ensure that each packet he or she produces carries a statement of the nicotine, tar and carbon monoxide yields of the cigarettes contained in it.
- (2) The statement –
- (a) as to the tar yield, shall be shown as a figure rounded to the nearest whole number and expressed in the form "x mg tar";
- (b) as to the nicotine yield, shall be shown as a figure rounded to one decimal place and expressed in milligrams in the form "x.y mg nicotine";
- (c) as to the carbon monoxide yield, shall be shown as a figure rounded to the nearest whole number and expressed in the form "x mg carbon monoxide".
- (3) The statement of the yields shall –
- (a) be printed on one side of the packet; and
- (b) cover an area amounting to at least 10% of that side of the packet.

**5 Appearance of written warning notices and yield statements**

A producer of a packet of tobacco shall ensure, in relation to each packet of tobacco produced by him or her, that the written warning notice required under Regulation 2(1)(a) and any statement required under Regulation 4 comply with the requirements of Schedule 2.

**6 Descriptions on packets**

No person shall produce or supply a packet of tobacco the packaging of which carries any name, brand name, text, trademark or pictorial or any other representation or sign which suggests that the tobacco it contains is less harmful to health than other tobacco.

**7 Imports from EEA states**

A person who imports into Jersey any packet of tobacco from an EEA State with a view to that tobacco being supplied for consumption in Jersey shall be regarded as complying with Regulations 3, 4 and 5 or any of them, if the packet complies with Article 5 of Directive 2001/37/EC of the European Parliament and of the Council of 5th June 2001 on the approximation of the laws, regulations and administrative provisions of the member States concerning the manufacture, presentation and sale of tobacco products (O.J. No. L 194 18.7.2001, p.26) as amended up to 7th August 2009<sup>3</sup> and with any requirements imposed by that EEA State pursuant to that Directive.

**8 Offences**

Any person who contravenes Regulation 2, 3, 4, 5 or 6 shall be guilty of an offence and liable to a fine of level 4 on the standard scale.

**9 Transitional provisions**

These Regulations shall not apply to any producer or supplier in respect of a packet of tobacco in existence before the date that these Regulations come into force, such packet –

- (a) in the case of a packet of cigarettes, being supplied to an end user before the date that is 12 months after the date that these Regulations come into force; and
- (b) in the case of any other packet of tobacco, being supplied to an end user before the date that is 24 months after the date that these Regulations come into force.

**10 Citation and commencement**

- (1) These Regulations may be cited as the Restriction on Smoking (Warning Notices) (Jersey) Regulations 2011.

- (2) These Regulations shall come into force 7 days after they are made.

**M.N. DE LA HAYE**

*Greffier of the States*

**SCHEDULE 1**

(Regulation 2)

**PICTURE WARNING NOTICES**

Note

- (1) All photographs, images and textual illustrations (© European Community) in this Schedule have been developed for use on tobacco packets in accordance with Commission Decision of 5th September 2003 (2003/641/EC) on the use of colour photographs or other illustrations as health warnings on tobacco packages<sup>4</sup> (O.J. No. L 226 10.9.2003, p.24).
- (2) A CD with the required images and a European Commission guidance document on editing the images is available from the Department of Health and Social Services and is available by e-mailing [health\\_promotion@health.gov.je](mailto:health_promotion@health.gov.je) or writing to the Head of Health Improvement, Public Health Department, Le Bas Centre, St. Saviour's Road, St. Helier, Jersey, JE1 4HR.

**1 List of picture warning notices**

- (1) Smokers die younger



- (2) Smoking clogs the arteries and causes heart attacks and strokes



- (3) Smoking causes fatal lung cancer





- (4) Smoking is highly addictive, don't start



- (5) Stopping smoking reduces the risk of fatal heart and lung diseases



- (6) Smoking can cause a slow and painful death



- (7) Smoking causes ageing of the skin



- (8) Smoking can damage the sperm and decreases fertility



- (9) Smoking may reduce the blood flow and cause impotence



- (10) Smoking contains benzene, nitrosamines, formaldehyde and hydrogen cyanide



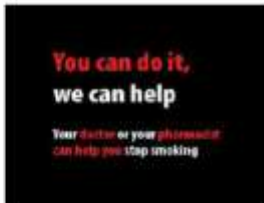
- (11) Smoking when pregnant harms your baby



- (12) Protect children: don't make them breathe your smoke



- (13) Your doctor or your pharmacist can help you stop smoking



- (14) Get help to stop smoking



**2 Alternative picture warning notice for travel retail sector**

Your doctor or your pharmacist can help you stop smoking.



**3 Technical specifications**

- (1) Each picture warning notice shall be surrounded by a black border outside the area specified in Regulation 3 which shall –
  - (a) be not less than 3 mm and more than 4 mm in width; and
  - (b) not interfere with the picture warning notice.
- (2) In the case of packets of cigarettes, each picture warning notice shall be irremovably printed on the packet.
- (3) In the case of packets of tobacco other than packets of cigarettes, each picture warning notice may be either irremovably printed on the packet or affixed to the packet by means of an irremovable sticker.
- (4) Subject to sub-paragraph (5), each picture warning notice shall –
  - (a) be in the format and proportions of the pictures and text set out in paragraph 1 or 2, as the case requires, and adopt the graphical integrity of those pictures and text;
  - (b) occupy the entire area reserved for the picture warning notice;
  - (c) be positioned parallel to the top edge of the packet, and in the same direction as the other information on the packet; and
  - (d) be printed in four-colour/-CMYK-/screen 133 lines per inch, as a minimum requirement.
- (5) Where the size of the packet so requires, the picture warning notice can be modified according to the following rules –
  - (a) the graphical editing of the textual elements shall be done by varying the font size and line breaks to ensure high readability;
  - (b) for picture warning notices where the illustration is a text, the graphical editing shall be done by varying font size and line breaks, however the relative surfaces occupied by text as an illustration and the corresponding text of the picture warning notice must be respected;
  - (c) for picture warning notices where a photograph or other illustration is an image, the graphical editing shall be done by proportionate scaling of the photograph or other illustration and varying of the relative surfaces occupied by the photograph or other illustration and the corresponding text of the picture warning notice;

- (d) when the proportion between the height and the width of the picture warning notice is lower than 0.8, the corresponding text of the picture warning notice, if placed under the photograph or other illustration in paragraph 1 or 2, may be moved to the right of the photograph or other illustration; and
  - (e) when the proportion between the height and the width of the picture warning notice exceeds 1.2, the corresponding text of the picture warning notice, if placed to the side of the photograph or other illustration in paragraph 1 or 2, may be moved under the photograph or illustration.
- (6) A picture warning notice must not –
- (a) be printed on the tax stamps on any packet of tobacco;
  - (b) be hidden, obscured or interrupted by –
    - (i) other written or pictorial matter, or
    - (ii) the opening of the packet.



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**SCHEDULE 2**

(Regulation 5)

**APPEARANCE OF WRITTEN WARNING NOTICE AND YIELD  
STATEMENT**

**1 Requirements**

- (1) The written warning notice required under Regulation 2(1)(a) and the yield statement required under Regulation 4 shall be –
  - (a) indelible;
  - (b) legible;
  - (c) printed in black Helvetica bold type on a white background;
  - (d) in a font size consistent throughout the text which ensures that the text occupies the greatest possible proportion of the area specified in Regulation 3(1)(a) or Regulation 4(3)(b);
  - (e) in lower case type, except for the first letter of the text;
  - (f) centred in the area in which the text is required to be printed, parallel to the top edge of the packet;
  - (g) surrounded by a black border outside the area specified in Regulation 3(1)(a) or Regulation 4(3)(b) being a border which shall –
    - (i) be not less than 3 mm and not more than 4 mm in width, and
    - (ii) not interfere with the text of the written warning notice or the yield statement, as the case requires; and
  - (h) subject to paragraph 2, be irremovably printed on the packet.
- (2) In the case of packets of tobacco other than cigarettes, the written warning notice required under Regulation 2(1)(a) and the yield statement required under Regulation 4 may be affixed to the packet by means of an irremovable sticker.
- (3) The written warning notice and yield statement must not –
  - (a) be printed on the tax stamps on any packet of tobacco; or
  - (b) be hidden, obscured or interrupted by –
    - (i) other written or pictorial matter, or
    - (ii) the opening of the packet.