

A WIN-WIN SOLUTION FOR OHIO'S HEALTH AND ECONOMY

**RAISE THE TOBACCO TAX TO FUND ECONOMIC STIMULUS
AND PRESERVE TOBACCO PREVENTION PROGRAMS**

**(INSTEAD OF RAIDING TOBACCO SETTLEMENT FUNDS
FROM OHIO'S TOBACCO PREVENTION PROGRAM)**

A Special Report by the Campaign for Tobacco-Free Kids

April 2008

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The Campaign for Tobacco-Free Kids is an independent, nonprofit organization dedicated to preventing and reducing tobacco use and its harms, especially among youth. The Campaign does not receive or accept any government funding, nor does it receive or accept any funding from the tobacco industry. To save lives and protect the public health, the Campaign supports efforts to increase tobacco tax rates throughout the country in order to reduce smoking, save lives, and reduce smoking-caused harms and costs. For more information, see www.tobaccofreekids.org.

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EXECUTIVE SUMMARY

Governor Strickland and the Ohio Legislature are currently trying to raid \$230 million from the Ohio Tobacco Prevention Foundation, which would basically end the state's programs to prevent children from starting to smoke and help smokers quit. Right now, while the matter is tied up in the courts, the Governor and the State Legislature could consider readily available alternative means to obtain the money they want – without causing all the unnecessary economic harm and public health damage that would come from taking needed funds away from the Tobacco Prevention Foundation.

By increasing Ohio's tobacco tax rates, the state could not only raise the desired \$230 million for Governor Strickland's economic stimulus package, it could also fully fund Ohio's tobacco prevention program (instead of killing it) and lock in substantial annual state revenue increases that would continue for years to come. This would produce sharp declines in tobacco use and its harms and costs in Ohio – instead of all the smoking increases, productivity declines, and higher levels of smoking-caused disease, death, and costs that would come from taking the \$230 million from the state's Tobacco Prevention Foundation.

The Ohio Tobacco Prevention Foundation has been doing a terrific job – and needs to keep working. Since it was created with state tobacco settlement funds in 2000, the Tobacco Prevention Foundation has helped to reduce Ohio's adult smoking rates by 12.2 percent, high school smoking rates by 38 percent, and middle school smoking by 47 percent. Thanks to those smoking declines, there are now more than 400,000 fewer adult smokers and 100,000 fewer youth smokers in Ohio, and more than 350,000 Ohio kids have been saved from growing up to become addicted adult smokers. These declines translate into state healthcare savings of more than \$6.1 billion. At the same time, the tobacco use declines produced by the Tobacco Prevention Foundation's work has increased worker productivity in the state, reduced business costs, and decreased demands on the state's Medicaid program.

Nevertheless, tobacco use and its toll are still way too high in Ohio, and the Foundation's continued efforts are desperately needed. Despite recent progress, 18,600 people still die each year in Ohio because of smoking, 20,800 kids become new, addicted smokers each year, and, every year, the state's government, businesses, and households spend more than \$4.3 billion on smoking-caused health care costs. In fact, the U.S. Centers for Disease Control and Prevention (CDC) estimates that smoking-caused health costs and productivity losses in Ohio total more than \$9.19 per pack sold in the state.*

Taking funding away from the Ohio Tobacco Prevention Foundation is shortsighted and will hurt the state and its residents. Despite all the Foundation's good works and the need for its continued efforts, the Governor and the state legislature are trying to take away nearly all of its available funds, virtually ending all state efforts to prevent and reduce tobacco use in Ohio. Such a money grab would be taking back tobacco settlement funds that were meant to be used for tobacco prevention and cessation programs and which the state government formally had dedicated to that purpose in prior years. Taking back that money would also destroy the existing infrastructure of programs and initiatives in Ohio that are working effectively to keep the state's tobacco use levels down and reduce them even further. Using conservative, research-based estimates, taking the \$230 million from the Ohio Tobacco Prevention Foundation would increase the number of current high school smokers by 8,200, increase the number of Ohio kids who will

* For more detail on the toll of tobacco in Ohio, see Appendix A.

become addicted smokers by 56,700, increase the number of Ohioans dying prematurely from smoking by 23,200, and increase future healthcare costs in the state by \$992.2 million.

Increasing Ohio's tobacco tax rates can easily raise \$390.8 million – not just the amount for the economic stimulus package, but more than enough to fully fund the state's tobacco prevention and cessation efforts and help address state budget deficits. For example, a 75-cent per pack increase in Ohio's cigarette tax rate, coupled with a parallel increase to the state's currently very low tax rate on other tobacco products (to 85 percent of wholesale price), would in just the first year produce the \$230 million desired by the Governor and the Legislature plus another \$100 million to bring state tobacco prevention and cessation funding to the level recommended by the CDC, with at least \$50 million left for general revenue purposes. Even with ongoing smoking declines, in future years the new revenues from the new tobacco tax rates would produce at least \$300 million for general revenues while still fully funding the state tobacco prevention program.

Ohio voters strongly support raising the state's tobacco tax rates and fully funding tobacco prevention and cessation efforts. In the past, Ohio residents and voters have expressed strong support for both raising state tobacco tax rates and for allocating funds to expanded tobacco prevention efforts. For example, in a 2004 poll, 69 percent of likely voters in Ohio supported a 75-cent cigarette tax increase, with even stronger support if part of the revenues were directed to increase state tobacco control efforts and health care.

Increasing the tobacco tax and fully funding tobacco prevention and cessation programs would produce substantial public health and economic benefits for the state. Not only would a 75-cent cigarette tax increase and an increase in the tax on other tobacco products produce enormous tobacco use declines and related public health and economic benefits, but fully funding Ohio's tobacco prevention and cessation efforts at the CDC-recommended level for Ohio would multiply the effect of the tobacco tax increase to its fullest extent, including the following:

- Preventing more than 239,400 Ohio kids from becoming addicted adult smokers – 112,000 from a tobacco tax increase and 127,400 from a fully-funded prevention program
- Prompting more than 120,500 current adult smokers to quit for good – 55,200 from a tobacco tax increase and 65,300 from a fully-funded prevention program
- Saving more than 108,400 Ohio citizens from dying prematurely from smoking – 50,400 due to a tobacco tax increase and 58,000 from a fully-funded prevention program
- Improving worker productivity throughout the state by reducing worker smoking
- Cutting future public, private sector, and household health costs by more than \$4.6 billion – \$2.4 billion from a tobacco tax increase and \$2.2 billion from a fully-funded prevention program
- Reducing future state Medicaid program expenditures caused by smoking by more than \$835 million – \$440 million from a tobacco tax increase and \$395 million from a fully-funded prevention program

The parallel increase to the state's tax rate on other tobacco products would produce even more public health and economic benefits for Ohio. Among other things, a higher tax rate on other tobacco products would reduce the number of kids using smokeless tobacco by 44.2 percent and cut overall consumption by about 23.8 percent – thereby reducing the death, oral cancers and other health problems caused by smokeless use.

GOVERNOR STRICKLAND'S PROPOSAL vs. THE TOBACCO TAX ALTERNATIVE
A Comparison of the Fiscal, Economic, and Public Health Impacts

	Gov. Strickland's Proposal	Tobacco Tax & Fully-Funded Prevention Program Alternative
New Money Available to the State in First Year	\$230 million	\$390 million
Is Additional New Funding Available Each Subsequent Year?	No	Yes
High School Smoking	Up 6.2%	Down 26.2%
Number of Current High School Smokers	8,200 More	34,800 Less
Number of Ohio Kids Alive Today Who Will Become Addicted Adult Smokers	56,700 More	239,400 Less
Number of Ohio Kids Alive Today Who Will Die Early from Smoking	18,100 More	76,500 Less
Number of Current Adult Smokers	19,400 More	120,500 Less
Number of Adults Who Will Die from Smoking	5,100 More	31,900 Less
Future Government, Business and Household Healthcare Costs in State	\$992.2 million Increase	\$4.6 billion Decrease
Future State Medicaid Program Expenditures	\$175.8 million Increase	\$835.6 million Decrease

Governor Strickland's Proposal is the effort currently underway to take back \$230 million in previously allocated tobacco settlement funds from the Ohio Tobacco Prevention Foundation, which will immediately curtail all state tobacco prevention program efforts and almost completely eliminate them within the next couple of years.

The Tobacco Tax & Fully-Funded Prevention Program Alternative would raise the state's cigarette tax by 75-cents per pack and increase the state's tax rate for other tobacco products to a parallel rate (85 percent), thereby not only providing the one-time \$230 million the Governor and Legislature want but also providing enough additional new revenue annually to fully fund the state's tobacco prevention and cessation efforts at the level recommended by the U.S. Centers for Disease Control and Prevention (CDC). This proposal also provides substantial additional new annual revenues to further strengthen Ohio's budget and avoid future budget deficits.

Sources

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This report shows that increasing Ohio's tobacco tax rates, instead of raiding funds from the Ohio Tobacco Prevention Foundation, would provide the \$230 million the Governor and Legislature want without hurting the state's current efforts to reduce tobacco use and its harms. In addition, the tobacco tax increase would establish a new stream of additional annual state revenues that would fully fund Ohio's tobacco prevention and cessation efforts at CDC-recommended levels and also greatly strengthen the state's budgetary and fiscal health.

While the Governor's proposal would be a step backward, producing increases to the number of adult and youth smokers and sharp related increases to healthcare costs, the tobacco tax alternative would produce brand new tobacco use reductions and related new cost savings.

Raid of Foundation Funds Will Increase Tobacco Use, Related Harms, and Costs

The plan to take the Foundation's money is short-sighted, only providing money to the state for one year, during which more than 20,000 kids will experiment with and become addicted to tobacco. This proposal will handicap the state with higher health costs and lower business productivity.

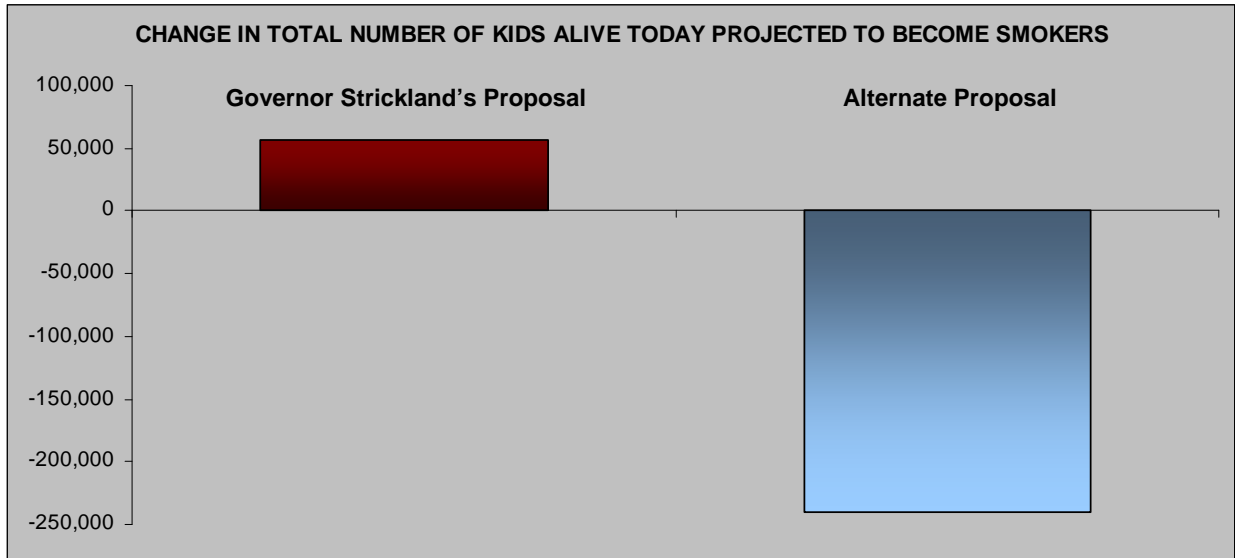
Since its creation in 2000, the Ohio Tobacco Prevention Foundation has helped to reduce Ohio's adult smoking rates by 12.2 percent, high school smoking rates by 38 percent, and middle school smoking by 47 percent. Those smoking declines translate into at least 400,000 fewer adult smokers and 100,000 fewer youth smokers in Ohio, and more than 350,000 Ohio kids saved from growing up to become addicted adult smokers. These declines amount to state healthcare savings of more than \$6.1 billion.¹ Without adequate resources, the Foundation cannot effectively reduce tobacco use, and Ohio's businesses will suffer as a result.

Studies show that smoking and other tobacco use decrease business productivity through high rates of absenteeism and reduced concentration and drive up businesses' health and non-health costs. With adequate funding, the Foundation can not only protect kids from tobacco addiction, but can ensure that the state will have healthy employees for successful businesses. Furthermore, reducing smoking among current adult smokers – Ohio's current employees and employers – makes businesses more productive and healthier.

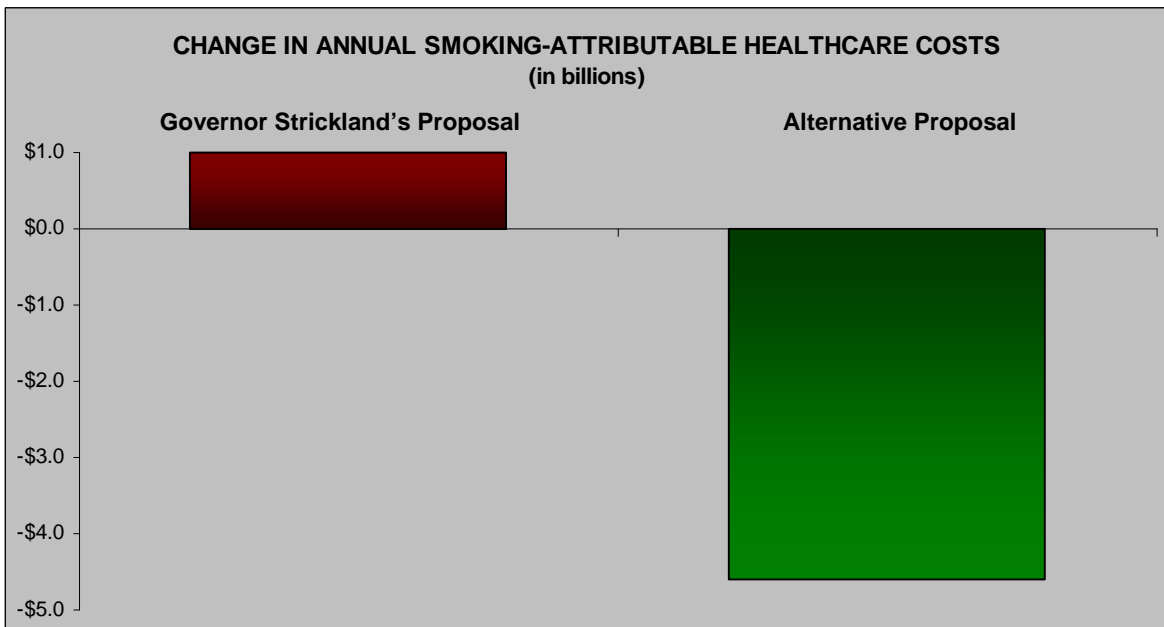
Ohio can expect the following increases in tobacco use and related costs from raiding the Foundation and stripping it of its ability to work effectively:²

<i>Increase in youth smoking</i>	6.2%
<i>Increase in number of current high school smokers</i>	8,200
<i>Increase in total number of kids alive today who will become smokers</i>	56,700
<i>Increase in number of kids alive today who will suffer from premature smoking-caused death</i>	18,100
<i>Increase in number of adult smokers</i>	19,400
<i>Increase in number of adults who will die from smoking</i>	5,100
<i>Increase in net total state healthcare costs due to increased smoking</i>	\$992.2 million
<i>Increase in net total state Medicaid program expenditures</i>	\$175.8 million

The chart below shows how youth smoking rates are projected to increase if the Foundation's funding is virtually eliminated, compared to the dramatic declines expected as a result of a fully-funded tobacco prevention and cessation program with a tobacco tax increase.³



The following graph shows how Governor Strickland's proposal will actually increase annual healthcare costs, whereas the alternative proposal presented here will decrease those costs.⁴



An Alternative Proposal Will Produce More Than Enough State Funds While Improving Public Health

Instead of raiding the Foundation's funds, which would have detrimental effects on Ohio's public health and Ohio, a much more reasonable and productive option is to increase the state's cigarette tax by 75 cents and the tax rate on other tobacco products to a comparable rate and fully fund tobacco prevention and cessation programs. Increasing the tobacco tax rates would produce enough revenue to support Governor Strickland's economic stimulus package, provide \$100 million to fully fund the Foundation's programs, and still have more than \$50 million left for

other state programs. This alternate option will dramatically improve the health of Ohioans, and because the state will continue to collect tobacco tax revenue at this new level for years to come, unlike the Governor’s proposal that would provide the state with money for just one year, the health and economic benefits would continue to grow every year these policies are in place.

The table below shows how Ohio’s state funds would remain high in the next years with the alternate option – even if tobacco use drops sharply – especially when compared to Governor Strickland’s one-year funding option. These projections assume a four percent decline in tobacco use due to fully-funded tobacco prevention and cessation programs and higher tobacco tax rate, as well as declines in healthcare costs associated with tobacco use.

	Year 1	Year 2	Year 3	Year 4	Year 5
Governor Strickland’s Proposal	\$230	\$0	\$0	\$0	\$0
Increasing Tobacco Taxes with a Fully-Funded Tobacco Prevention Program	\$390.8	\$375.2	\$360.2	\$345.8	\$331.9

Increasing Ohio’s tobacco tax rates will produce \$390.8 million in new state revenues. By increasing Ohio’s current cigarette tax rate by 75 cents per pack, the state would collect more than \$310.5 million in new revenue in just the first year. A corresponding increase in the state’s tax rate on other tobacco products to parallel the new cigarette tax rate would earn an additional \$80.3 million in new revenue – for a total of \$390.8 million.

Ohio last increased its cigarette tax in 2005, to \$1.25 per pack, placing its rate 21st highest out of the 50 states and DC. If Ohio increases its cigarette tax rate by 75 cents, it will be joining 10 other states that now have cigarette tax rates of \$2.00 or higher. New York will have the highest state rate when its new \$2.75 per pack goes into effect in June 2008.

Right now, Ohio’s tax on all other tobacco products is 17 percent of the wholesale price, which is among the lowest rates in the U.S., and is at a significantly lower rate than the cigarette tax. Considerably lower tax rates and prices for other tobacco products compared to cigarettes make it easier for kids to use the cheaper tobacco products as a gateway to a lifetime of tobacco addiction.* Massachusetts, Maine, Alaska, and Minnesota have the highest taxes of 90 percent, 78 percent, 75 percent, and 70 percent of the wholesale price, respectively. An increase to Ohio’s OTP tax rate that parallels a \$2.00 cigarette tax rate increase would bring the rate to 85 percent of wholesale price. That rate increase would bring the state more than \$80.3 million in additional new annual tobacco tax revenues. Equally important, it would save lives and promote public health.

Implementing a minimum tax level for OTP with a percentage-of-price tax system would address concerns about bargain-priced products paying too little in taxes and bring in even more revenue for the state.

Massive amounts of economic research and state experiences have firmly established that significantly raising state tobacco tax rates will always substantially increase state revenues, despite the related declines in smoking and tobacco use and any related increases in cigarette smuggling or cigarette tax avoidance.† Put simply, the additional revenues the state receives per tobacco unit sold after a tobacco tax increase brings in far more revenue than the state

* See TFK Factsheet, *Benefits from Increasing Smokeless Tobacco Tax Rates*, <http://tobaccofreekids.org/research/factsheets/pdf/0180.pdf> and the references cited therein.

† See TFK Factsheets, *Raising State Cigarette Taxes Always Increases State Revenues (And Always Reduces Smoking)*, <http://www.tobaccofreekids.org/research/factsheets/pdf/0098.pdf> [and references cited therein], and *Raising Cigarette Taxes Reduces Smoking, Especially Among Kids (And the Cigarette Companies Know It)*, <http://www.tobaccofreekids.org/research/factsheets/pdf/0146.pdf>.

loses from the declines in sales prompted by the increase. For instance, in Ohio, cigarette tax revenue collections increased by 78.9 percent compared to a 20.6 percent decline in cigarette pack sales after the state's last cigarette tax rate increase of 70 cents in 2005.⁵

Revenues from the tobacco tax increase will help the state's fiscal health for this and future years. Year to year, state cigarette tax revenues are more predictable and less volatile than many other state revenue sources, such as state income tax or corporate tax revenues, which can vary considerably year to year because of nationwide recessions or state economic slowdowns. In sharp contrast, large drops in cigarette tax revenue from one year to the next are quite rare because of the addictive power of cigarettes. After a major cigarette tax increase, state tobacco tax revenues typically decline by only about two percent per year, on average, because of ongoing reductions in smoking levels. An increase in the state's tobacco tax rate would not only stop those revenue declines from occurring but would also bring in more than enough new annual revenue to offset those declines.*

The smoking and tobacco use declines behind those gradual revenue reductions would also simultaneously produce much larger reductions in government and private sector smoking-caused expenditures.† At the same time, the smokers and tobacco users who terminate or reduce their purchases of tobacco products will use the money they save to purchase other state goods and services, which will further strengthen the state's economy – and to the extent that such consumers purchase other goods subject to special state taxes (e.g., alcoholic beverages or gasoline), the decline in tobacco product sales will also increase those other forms of state revenue. In addition, there are a variety of other actions Ohio could take to protect and maintain, or even increase, its tobacco tax revenues over time. For instance, the state can periodically increase its tobacco tax rates or index its cigarette tax rate to inflation.‡

If passed by the legislation and signed by the Governor, a tobacco tax increase could be implemented within a month, which means that Ohio can collect greater revenues almost immediately. Making the rate increase effective as soon as possible would limit any actions that people may take to evade the new rate, such as purchasing products at the pre-increase price. In addition, it is important to include a floor stocks (inventory) tax in the legislation to ensure that the state will not lose revenue from products that are in wholesalers', distributors', and retailers' inventories when the increase goes into effect. The state can easily collect this tax by requiring wholesalers, distributors, and retailers to record their inventory at midnight before the new tobacco tax rate goes into effect.

Ohio residents strongly support increasing the state's tobacco tax rates and fully funding tobacco prevention efforts. In the past, Ohio residents and voters have expressed strong support for both raising state tobacco tax rates and for allocating funds to expanded tobacco prevention efforts. For example, in a 2004 poll, 69 percent of likely voters in Ohio supported a 75-cent cigarette tax increase, with even stronger support if part of the revenues were directed to increase state tobacco control efforts and health care.⁶

Increasing Ohio's tobacco tax rate and fully funding a tobacco prevention and cessation program will significantly reduce tobacco use and its related harms. A tobacco tax increase will also provide public health benefits in the long term. That, in addition fully-funding

* See TFK Factsheet, *Tobacco Tax Increases are a Reliable Source of Substantial New State Revenue*, <http://www.tobaccofreekids.org/research/factsheets/pdf/0303.pdf>.

† See, e.g., TFK Factsheet, *Benefits & Savings From Each One Percentage Point Decline in Adult and Youth Smoking Rates in the United States*, <http://tobaccofreekids.org/research/factsheets/pdf/0235.pdf>.

‡ See Appendix E for a detailed explanation on how Ohio can maximize its tobacco tax revenues by minimizing smuggling and other tax evasion. See also, TFK Factsheet, *State Options to Prevent and Reduce Cigarette Smuggling and to Block Other Illegal State Tobacco Tax Evasion*, <http://www.tobaccofreekids.org/research/factsheets/pdf/0274.pdf>.

the Foundation's prevention programs, will help Ohio in the long run by reducing the number of present and future smokers, saving lives, and saving the state millions in healthcare costs.

Significant tobacco tax increases – particularly for cigarettes – are the fastest way to sharply reduce tobacco use and, more importantly, smoking-caused disease, death, and costs. In addition, for every person who dies from smoking in the state, there are another 20 people suffering from smoking-caused disease or disability. Recent reports by the National Academy of Sciences' Institute of Medicine and the President's Cancer Panel have strongly recommended that states raise their tobacco tax rates to effectively reduce the toll that tobacco use takes on the states.⁷

Even the cigarette companies have repeatedly acknowledged, both publicly and in internal company documents disclosed in tobacco lawsuits, that raising cigarette prices through state tobacco tax increases significantly reduces smoking, especially among kids. For instance, in 1994, Ellen Merlo, Senior Vice President of Corporate Affairs for Philip Morris, stated, "When the tax goes up, industry loses volume and profits as many smokers cut back."⁸

Indeed, the actual experiences of the states that have raised their cigarette tax rates firmly establish that cigarette tax increases reduce smoking rates and related harms (while increasing revenue).^{*} In Ohio, for instance, cigarette consumption declined by more than 20 percent after its 2005 cigarette tax rate increase.⁹

Clearly, cigarette tax increases are one of the most effective ways to sharply reduce smoking, especially among youth, pregnant women, and low-income smokers. Studies have shown that for every 10 percent increase in the price of cigarettes, youth smoking drops by approximately 6.5 percent, smoking among pregnant women drops at a similar rate, and overall consumption declines by three to five percent.¹⁰

Increasing the state's tax on tobacco products to 85 percent of the wholesale price would reduce overall consumption by about 23.8 percent, while a 75-cent cigarette tax increase is projected to produce the following declines in smoking-affected pregnancies and overall consumption.

	5-Year Decline in Smoking-Affected Pregnancies	Fewer Cigarette Packs Sold
75-Cent Cigarette Tax Increase	17,600	136.6 million

Directing some of the new revenues from a tobacco tax rate increase to expand the state's efforts to prevent and reduce tobacco use would magnify the many public health benefits and cost benefits, described above, from the tobacco tax increase alone.

Unfortunately, Ohio currently falls short of the amount recommended by the U.S. Centers for Disease Control and Prevention (CDC) for state tobacco prevention spending: \$145 million per year. In fiscal year 2008, Ohio is spending \$44.7 million to prevent and reduce tobacco use and its many harms and costs. The Foundation thus far has made remarkable progress in lowering tobacco use rates in Ohio with the minimal funds it has been given.

Maintaining funding for the Foundation is crucial to reducing tobacco use in the state and to preventing a new generation of addicted tobacco users from starting. Rather than further cutting back on funds for this essential state program as proposed by Governor Strickland, it makes more economic sense to put a portion of the new revenues from a tobacco tax increase

^{*} See TFK Factsheets, *Raising Cigarette Taxes Reduces Smoking, Especially Among Kids (And the Cigarette Companies Know It)*, <http://www.tobaccofreekids.org/research/factsheets/pdf/0146.pdf>, and *Raising State Cigarette Taxes Always Increases State Revenues and Always Reduces Smoking*, <http://www.tobaccofreekids.org/research/factsheets/pdf/0098.pdf>.

towards prevention and cessation program funding to reach the CDC-recommended level and secure much more powerful public health benefits and related cost savings.

The alternate proposal will prevent more than 239,000 youth from becoming addicted tobacco users and save more than 76,500 youth from future smoking-caused deaths.

Applying these findings to a 75-cent increase to Ohio's cigarette tax rate shows that the state will enjoy the following benefits.

	Decline in Youth Smoking	Kids Alive Today Stopped From Smoking	Kids Saved From Dying From Smoking
75-Cent Cigarette Tax Increase	12.3%	112,100	35,800
Fully-Funded Prevention Program	13.9%	127,300	40,700
TOTAL	26.2%	239,400	76,500

Currently, 7.5 percent of high schoolers and 2.1 percent of middle schoolers in Ohio use smokeless tobacco. The habit is more popular among boys than girls, with 13.7 percent of high school boys using smokeless tobacco compared to 1.6 percent of high school girls.¹¹ Increasing the state's tax on tobacco products to 85 percent of the wholesale price would reduce the number of kids who use smokeless or spit tobacco by approximately 44.2 percent and reduce overall consumption by about 23.8 percent – with corresponding reductions to the death, disease, costs and other harms caused by these tobacco products.

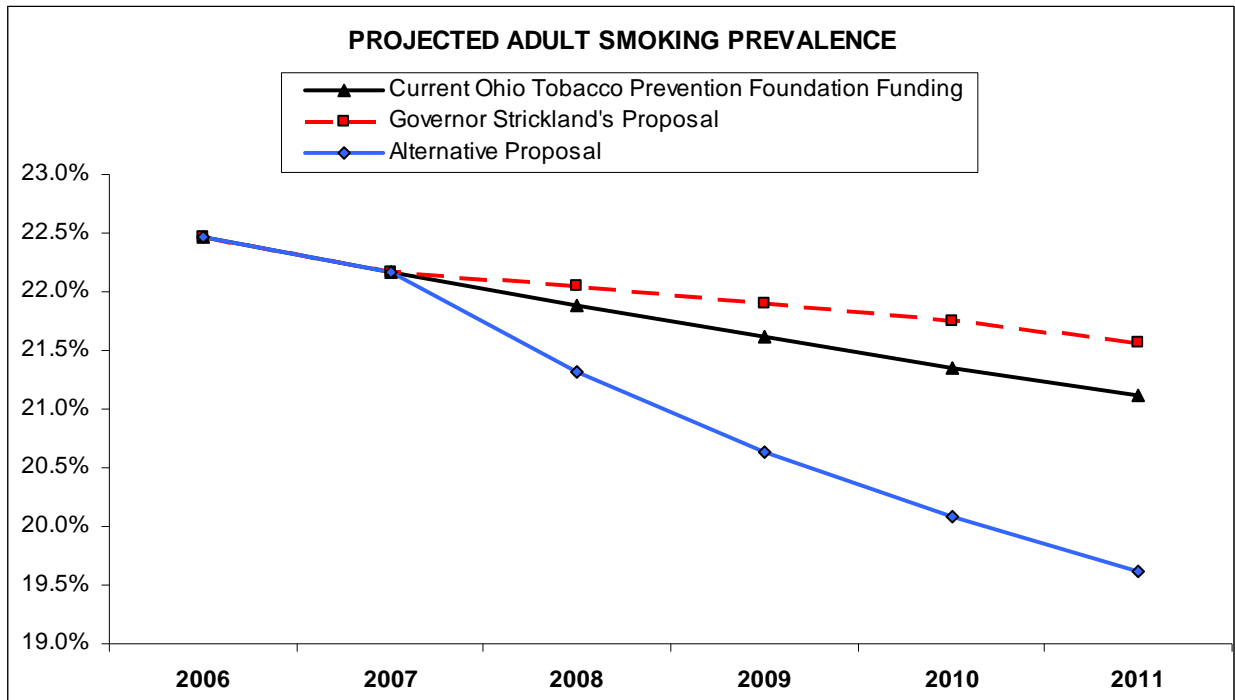
Recent data suggest that cigar smoking may be increasing among kids. In Ohio, 14.4 percent of high school students smoke cigars.¹² Raising the cigar tax in the state is an effective method to reduce cigar use, especially among youth. Cigars, particularly small cigars that look and weigh similar to cigarettes, currently are taxed at a lower rate than cigarettes. The best way to decrease cigar smoking levels and to increase revenues for the state is to increase the cigar tax at least to parallel that of cigarettes – 85 percent of the wholesale price.

Increasing the tax on these accessible products will discourage switching to lower-cost products and help to prevent youth from smoking cigars, which often come in kid-friendly flavors such as grape, cherry, and chocolate.

A 75-cent cigarette tax increase with a fully-funded tobacco prevention and cessation program would prompt 120,500 adults to quit smoking and save 31,900 adults from smoking-caused deaths. A tobacco tax increase and an effective tobacco prevention and cessation program would help many adult smokers quit. Many would quit in response to the price increase, which would prevent thousands of smoking-caused deaths.

	Adult Smokers Who Quit	Adults Saved From Dying From Smoking
75-Cent Cigarette Tax Increase	55,200	14,600
Fully-Funded Prevention Program	65,300	17,300
TOTAL	120,500	31,900

The following graph shows how, compared to fully funding the Ohio tobacco prevention and cessation program and increasing the state tobacco tax rates, raiding the Foundation's funds will cause adult smoking rates to stagnate.¹³



These results might seem extraordinary, but other states and localities that have raised their cigarette tax significantly have obtained similar results. The number of smokers is so large and the impact of smoking is so deadly that even small percentage declines in smoking produce dramatic health and cost savings.

Small tobacco tax increases and less investment in tobacco prevention will bring Ohio smaller public health and economic benefits. Smaller tobacco tax rate increases will, of course, produce smaller smoking or tobacco use declines and fewer related health benefits and cost savings than larger tobacco tax increases – and some small rate increases will not produce any smoking or tobacco use declines or health care benefits and savings at all. Indeed, the public health benefits and cost reductions from smaller rate increases are far from secure and much less certain than those obtained from robust rate increases.

Faced with relatively small cigarette tax increases, big cigarette companies can fairly easily mute or eliminate any related smoking declines and public health benefits by temporarily reducing their own prices and activating a range of temporary retailer-based discounts and promotions. In recent years, cigarette companies have increased the amount of product discounting (such as buy-one-get-one promotions) and the level of spending on such promotions after cigarette tax increases or even their own self-imposed price increases.¹⁴ As a result, any public health benefits due to higher prices of tobacco products, including lower levels of initiation by youth and higher quit rates, would be limited or nonexistent, compared to a higher rate increase, which the tobacco companies could not offset effectively.

The tobacco tax increase will make the rate more proportional to the price of tobacco products. Any cigarette company opposition to efforts to increase Ohio's cigarette tax is, of course, based entirely on the companies' desire to protect their own sales and revenues. They are happy to increase cigarette prices to maximize their own profits, but state cigarette tax increases reduce pack sales with all the new revenues going to the state rather than the companies. In fact, Ohio's cigarette tax rate has failed to keep up with the ongoing increases in cigarette prices in the state. Just since 1998, the average price of a pack of cigarettes has almost doubled, as the major cigarette companies have raised the prices they charge by more than \$1.00 per pack (more than twice the amount needed to cover all of their settlement-related

costs).^{*} While competitive pressure from new, small manufacturers' brands temporarily dampened these major company price hikes in recent years, the major cigarette companies announced a brand new price increase in September 2007 (the last price increases were just the year before), and Wall Street tobacco industry analysts expect more to come.¹⁵

Because of past industry pricing and state tax policies, the cigarette companies have been getting increasingly larger revenues and profits from each pack sold in the state while the state's share of cigarette revenues has become smaller and smaller. Right now, Ohio's cigarette tax currently accounts for about 29.7 percent of the average price of a pack of cigarettes in the state.¹⁶ In contrast, the cigarette companies receive about 54.1 percent of the money spent on cigarettes in Ohio.¹⁷ A 75-cent rate increase would make those shares of overall cigarette sales revenue more equal.

The cigarette companies also use a portion of their revenues from Ohio cigarette pack sales to maintain and increase smoking levels (and related harms and costs) in the state through extensive advertising and other marketing efforts. In 2005, the most recent year for which data is available, tobacco companies spent an estimated \$724.0 million on marketing and promotions in Ohio (which is about 71 cents per pack sold in the state in 2005). That represents a 101.5 percent increase since 1998, when the Master Settlement Agreement went into effect.¹⁸ Increasing Ohio's cigarette tax by at least 75 cents per pack and investing some of the new revenue to expand state tobacco prevention and cessation efforts is one way to offset the impact of the cigarette companies' marketing and promotional spending in the state.

The Tobacco Use Declines from this Alternate Proposal Will Reduce Public and Private Non-Health Costs

Governor Strickland's proposal is meant to increase employment within the state, but that option ignores the important factor of having a healthy pool of employees to fill those positions. Businesses want to hire productive employees who will contribute to the growth of the company – and, consequently, improve the state economy. Instead, by taking money away from the Foundation's programs to reduce tobacco use, which is a major contributor to decreased health and productivity, Governor Strickland seems to be undermining his own plan.

By reducing smoking and tobacco use, a tobacco tax increase with a fully-funded tobacco prevention and cessation program would reduce a range of non-healthcare costs throughout the state, such as the amount of property damage and loss from smoking-caused fires and smoking-caused cleaning and maintenance costs. But the biggest non-health-cost benefit might be the impact of the smoking declines on improving worker productivity and reducing related losses.

Considering Governor Strickland's main goal is to improve employment in Ohio, it would make sense to make a policy change that has been shown to increase state employment, increase worker productivity, and provide many other benefits to the state.

Increasing state employment and further strengthening Ohio's economy. Tobacco use contributes to higher absentee rates, more hospital visits, and greater risk of accidents and injuries.¹⁹ Thus, reducing tobacco use through tobacco tax increases and prevention and cessation programs would increase employment.

Evidence shows that increasing cigarette tax rates will help to increase overall state employment levels. For example, economic studies have found that even if smoking were entirely eliminated in the United States, the net economic effect on the states would be positive, with more jobs created as well as other increases in productive economic activity.²⁰ State-specific economic impact studies in New Hampshire, Texas, and Virginia have found that

^{*} See TFK Factsheet, *U.S. Cigarette Companies' Settlement-Related Price Hikes Excessive*, <http://tobaccofreekids.org/research/factsheets/pdf/0071.pdf>.

substantial cigarette tax increases in those states would actually increase total state employment – and that reduced cigarette sales have, in the past, been linked with increased state retail employment.²¹

One way that cigarette tax increases improve the economic activity in a state is that smokers who quit or cutback because of the increase use the money they formerly spent on cigarettes in other ways – and those alternative uses are likely to produce more jobs and more productive economic activity. For example, cigarette manufacturing and distributing is very capital intensive and does not create a lot of jobs for people; thus, shifts to spending on other goods and services that are more labor intensive will create jobs. Spending on cigarettes in states with little or no cigarette manufacturing also exports state consumer dollars to those other states. More generally, spending on cigarettes creates high social costs, but spending on less harmful consumables along with increased consumer savings or investments will be more socially constructive and more economically productive.*

Increasing Ohio's tobacco tax rates will create lasting improvements for employment rates and the economy while also contributing to a healthier workforce now and for future generations. Allocating some of the new revenue towards the Foundation will further solidify those public health benefits for the businesses and the state economy through lower health costs.

Reducing productivity losses in the state. Currently, the CDC estimates that the productivity losses in Ohio from productive work lives being shortened by smoking-caused death total more than \$4.7 billion each year.²² In addition, one study found that smoking hurts productivity because employees who smoke are absent from work on average 6.16 days per year due to illness, whereas nonsmokers are absent on average 3.86 days per year.²³ Similarly, a study done for the Indiana Health Department determined that the cost of smoking employees to businesses in just a single Indiana county totaled \$260.1 million per year from increased absenteeism and lost productivity, higher health insurance premiums, and increased recruitment and training costs from smoking employees' premature retirement and death.²⁴

By reducing smoking among workers, a tobacco tax increase and fully-funded prevention and cessation program would cut public and private sector employer productivity losses by improving worker health and on-the-job performance, reducing the amount of smoking-caused work absences and work-time cigarette breaks, and reducing the number of productive work years lost from smoking-caused illness or disability interrupting or prematurely ending healthy and productive work lives. A healthier, more productive workforce would not only help existing state government and business employers but would also make Ohio more attractive to businesses that may consider relocating to the state.

The Declines in Tobacco Use and Related Harms from the Alternate Option Will Reduce Government, Private Sector, and Household Smoking-Caused Health Costs

Extra healthcare expenditures in Ohio caused by smoking add up to more than \$4.4 billion annually, with the state Medicaid Program's share an estimated \$1.4 billion per year.[†] Increasing the state's cigarette tax rate by a substantial amount is one of the most effective methods to reduce these costs to Ohio's government, businesses, and taxpayers.

Businesses pay the majority of smoking-related healthcare costs. Studies have indicated that 30 to 85 percent of medical costs to employers are unnecessarily excessive and could be reduced if the health status of their employees was improved.²⁵ Each smoking employee costs their employer an estimated \$1,000 to \$4,600 per year in excess medical costs.²⁶

* For a full list of benefits to Ohio from a 75-cent cigarette tax increase, see Appendix B.

† For more detail on the economic toll of tobacco use in Ohio, see Appendix A.

As the table below shows, in the first five years, a 75-cent cigarette tax rate increase would reduce health care costs by \$58.9 million just from fewer smoking-caused heart attacks, strokes and fewer smoking-affected births.*

	5-Year Heart-Stroke Savings	5-Year Pregnancy Savings
75-Cent Cigarette Tax Increase	\$29.0 million	\$29.9 million

The pregnancy savings would start immediately, as the cigarette tax increase discourages pregnant women from smoking. The heart attack and stroke savings from the immediate smoking declines would start out small in the first year, but would then increase sharply each year until reaching a peak in eight to 10 years and then maintaining that high rate thereafter. In other words, the heart-stroke savings in the second five years would be substantially larger than the savings in the first five years. More importantly, these immediate heart-stroke and pregnancy cost reductions represent only the tip of the savings iceberg for Ohio, as the smoking declines from a 75-cent rate increase would immediately begin to reduce numerous other smoking-caused health costs as well.

The alternate proposal will save Ohio \$4.6 billion in total future healthcare costs, with \$835.6 million of those savings in the state Medicaid program. All of these savings would also help to reduce skyrocketing state Medicaid program costs because it covers approximately 17.7 percent of the state’s total smoking-caused health costs and 50 percent of smoking-caused pregnancy-related health costs in the state.²⁷

	Total Future Health Savings	Medicaid Share of Total Savings
75-Cent Cigarette Tax Increase	\$2.4 billion	\$440.5 million
Fully-Funded Prevention Program	\$2.2 billion	\$395.1 million
TOTAL	\$4.6 billion	\$835.6 million

The overall healthcare savings to public, private sector, and household healthcare costs throughout the state would occur over the lifetimes of the smokers who quit or kids who never start smoking because of a 75-cent increase and a fully-funded tobacco program. Besides Medicaid, Ohio would also see reductions to the smoking-caused health costs in other state or state-funded programs because of the smoking declines prompted by the cigarette tax increase – and private sector and individual smoking-caused health costs would also decline. Most notably, decreasing smoking rates among workers would also lower public and private sector employers’ health care and health insurance costs.

The Alternative Option Will Help Low-Income Residents

One of the most frequent attacks made by the big tobacco companies against large tobacco tax increases is that they unfairly burden lower-income smokers. In fact, tobacco tax increases are one of the most effective ways of reducing the massive regressive burden caused by smoking on lower-income households and communities.†

* For a full list of benefits to Ohio from a 75-cent cigarette tax increase, see Appendix B. For detailed information and references regarding how these projections were made, see Appendix D.

† For more on the many benefits to lower-income persons and families from cigarette tax increases, see TFK Factsheet, *State Cigarette Tax Increases Benefit Lower-Income Smokers & Families*, <http://tobaccofreekids.org/research/factsheets/pdf/0147.pdf>.

Put simply, the death, harm, disability, and suffering caused by smoking are currently focused much more in lower-income families and communities because smoking levels are higher among lower-income than among higher-income persons, and lower-income persons have less access to health care, cessation assistance, and other treatment. Tobacco tax increases help to reduce this horrible burden among lower-income families and communities both by prompting current lower-income smokers and tobacco users to quit and by preventing lower-income kids from starting. Moreover, because lower-income smokers are more likely to quit or cutback in response to tobacco tax increases than higher-income smokers, the household public health and economic benefits from tax-prompted smoking declines are enjoyed predominantly by those with lower-incomes.²⁸

More than one-third of those expected to quit in Ohio have incomes below 200 percent of the poverty line and more lower-income smokers would quit in response to a significant cigarette tax increase compared to higher-income smokers: more than 19,500 lower-income smokers would quit in response to the 75-cent rate increase compared to more than 4,500 higher-income smokers. Additionally, quitting would lead to roughly 5,000 fewer smoking-caused deaths among lower-income adults and roughly 1,000 fewer smoking-caused deaths among higher-income adults.

Lower-income smokers who quit or cutback because of a state cigarette tax increase will also secure an enormous “tax cut.” A smoker who quits or cuts back not only avoids the cigarette tax increase on each pack he or she no longer smokes but also avoids the original state tax and saves all the other money previously paid for each pack. In Ohio, a pack-a-day smoker who quits because of a 75-cent cigarette tax increase would save more than \$1,800 per year from no longer buying cigarettes – with additional savings from avoiding other smoking-caused costs.* And smokers who quit or cut back in Ohio would save more than \$550 million all together.

Given the consistently strong support for cigarette tax increases among low-income persons and the enormous benefits those tax increases bring to low-income smokers, families, and communities, the big cigarette companies’ efforts to “protect” low-income communities from higher cigarette taxes is not only patronizing and misdirected but also hostile to lower-income interests.†

Conclusion

While the Governor proposes to deplete the funds of a proven-effective tobacco prevention and cessation program for one-year’s worth of money for his economic stimulus package, an alternative option would not only raise more than enough money for that proposal, but also would produce additional public health benefits. Increasing the state cigarette tax rate to \$2.00 per pack and the tax rate on other tobacco products to 85 percent of the wholesale price, and fully funding the state’s tobacco prevention and cessation program would raise \$390.8 million – more than enough revenue for the Governor’s economic stimulus package without sacrificing the health of Ohio’s citizens, and especially Ohio’s kids. The people, businesses, and taxpayers of Ohio deserve no less.

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* The current average price for cigarettes in Ohio is \$4.21 per pack (including sales tax), and adding a 75-cent cigarette tax increase will raise that average price to about \$5.00 per pack (including sales tax). \$5.00 times 365 days in a year equals \$1,825 in annual savings to a pack-a-day smoker who quits (or to a heavier smoker who reduces his or her consumption by a pack a day).

† For an analysis of the other self-serving arguments commonly made against tobacco tax increases by the cigarette companies and their allies, see TFK Factsheet, *Responses to Misleading and Inaccurate Cigarette Company Arguments against State Tobacco Tax Increases*, <http://tobaccofreekids.org/research/factsheets/pdf/0227.pdf>.

APPENDIX A

THE TOLL OF TOBACCO IN OHIO

Tobacco Use in Ohio

- High school students who smoke: 20.5% [Girls: 20.8% Boys: 20.0%]
- High school males who use smokeless tobacco: 13.7%
- Kids (under 18) who try cigarettes for the first time each year: 67,500
- Additional Kids (under 18) who become new regular, daily smokers each year: 20,800
- Packs of cigarettes bought or smoked by kids in Ohio each year: 26.8 million
- Kids exposed to second hand smoke at home: 919,000
- Adults in Ohio who smoke: 23.1% [Men: 24.9% Women: 20.2% Pregnant Females: 17.9%]

Nationwide, youth smoking has declined significantly since the mid-1990s, but that decline appears to have slowed or even reversed. The 2005 Youth Risk Behavior Survey found that the percentage of high school students reporting that they have smoked cigarettes in the past month increased to 23 percent in 2005 from 21.9 percent in 2003. 20.8 percent of U.S. adults (about 45 million) currently smoke, about the same as the 20.9 percent who smoked in 2004 and 2005.

Deaths in Ohio From Smoking

- Adults who die each year in Ohio from their own smoking: 18,600
- Adult nonsmokers who die each year from exposure to secondhand smoke: 1,070 to 3,000
- Ohio kids who have lost at least one parent to a smoking-caused death: 10,100
- Kids alive in state today who will ultimately die from smoking: 293,000 (given current smoking levels)

Smoking, alone, kills more people each year than alcohol, AIDS, car crashes, illegal drugs, murders, and suicides combined. For every person in Ohio who dies from smoking approximately 20 more state residents are suffering from serious smoking-caused disease and disability, or other tobacco-caused health problems.

Tobacco-Related Monetary Costs in Ohio

- Annual health care expenditures in the State directly caused by tobacco use: \$4.37 billion
- Annual health care expenditures in Ohio from secondhand smoke exposure: \$205.3 million
 - State Medicaid program's total health expenditures caused by tobacco use: \$1.4 billion
- Citizens' state/federal taxes to cover smoking-caused government costs: \$2.8 billion (\$638/household)
- Smoking-caused productivity losses in Ohio: \$4.65 billion
- Smoking-caused health costs and productivity losses per pack sold in Ohio: \$9.19

The productivity loss amount, above, is from smoking-death-shortened work lives, alone. Additional work productivity losses totaling in the tens of billions nationwide come from smoking-caused work absences, on-the-job performance declines, and disability during otherwise productive work lives. Other non-health costs caused by tobacco use include direct residential and commercial property losses from smoking-caused fires (about \$400 million nationwide); and the costs of extra cleaning and maintenance made necessary by tobacco smoke and tobacco-related litter (about \$4+ billion per year for commercial establishments alone).

Tobacco Industry Advertising and Other Product Promotion

- Annual tobacco industry marketing expenditures nationwide: \$13.4 billion (\$36+ million per day)
- Estimated portion spent in Ohio each year: \$724.0 million

Published research studies have found that kids are three times more sensitive to tobacco advertising than adults and are more likely to be influenced to smoke by cigarette marketing than by peer pressure, and that one-third of underage experimentation with smoking is attributable to tobacco company marketing.

Ohio Government Policies Affecting The Toll of Tobacco in Ohio

- Annual State tobacco prevention spending from tobacco settlement and tax revenues: \$44.7 million [National rank: 14 (with 1 the best), based on percent of CDC recommendation]
- State cigarette tax per pack: \$1.25 [National rank: 21st (average state tax is \$1.14 per pack)]

Sources

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APPENDIX B

BENEFITS FROM A 75-CENT CIGARETTE TAX INCREASE IN OHIO

Current State Cigarette Tax: 125 Cents Per Pack (21st among all states)

Smoking-caused costs in Ohio per taxed pack sold: \$9.19

Average retail price per pack: \$4.21 (state share from excise and sales taxes: \$1.49)

Annual health care expenditures in Ohio directly caused by tobacco use: \$4.37 billion

Total state Medicaid program smoking costs each year: \$1.40 billion

Annual state cigarette tax revenue: \$955.2 million (2007)

Projected Benefits from Increasing the State Cigarette Tax by 75 Cents Per Pack

- **New state cigarette tax revenues each year: \$310.5 million**
- **Pack sales decline in state: -136.6 million**
- **Percent decrease in youth smoking: 12.3%**
- **Increase in total number of kids alive today who will not become smokers: 112,100**
- **Number of current adult smokers in the state who would quit: 55,200**
- **Number of smoking-affected births avoided over next five years: 17,600**
- **Number of current adult smokers saved from smoking-caused death: 14,600**
- **Number of kids alive today saved from later premature smoking-caused death: 35,800**
- **5-Year healthcare savings from fewer smoking-affected pregnancies & births: \$29.9 million**
- **5-year healthcare savings from fewer smoking-caused heart attacks & strokes: \$29.0 million**
- **Long-term healthcare savings in state from adult & youth smoking declines: \$2,486.2 million**

These projections are based on research findings that a 10% cigarette price increase reduces youth smoking rates by 6.5%, adult rates by 2%, and total consumption by 4% (but adjusted down to account for tax evasion effects), and assume that the state tax will keep up with inflation. Nevertheless, the tax increase will both reduce smoking levels and increase state revenues because the higher tax per pack brings in more new revenue than is lost from the drop in the number of packs sold. These projections are fiscally conservative because they include a generous adjustment for lost state pack sales (and tax revenues) from new tax avoidance efforts after the tax increase by continuing in-state smokers. Projected new revenue amounts are for net new revenues above the actual cigarette tax revenues received by the state in the year preceding the tax increase. Without any tax increase, it is likely that the revenues would decline by a small amount. Kids stopped from smoking and dying are from all kids alive today. Long-term savings accrue over lifetimes of persons who stop smoking or never start because of tax increase. These projections assume that the state will follow standard practice and apply the cigarette tax increase to all previously tax-stamped or otherwise tax-paid cigarettes held in inventory by wholesalers or retailers on the effective date of the increase. Failing to tax such cigarettes held in inventory would open the door to massive pre-increase stockpiling by retailers and wholesalers to evade the increase, drastically reducing the amount of new state revenues. All cost and savings amounts are in 2004 dollars.

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APPENDIX C

BENEFITS & SAVINGS FROM EACH ONE PERCENTAGE POINT DECLINE IN OHIO'S SMOKING RATES

The following estimates show the benefits and savings that are obtained in Ohio for each one percentage point decline in adult and youth smoking rates in the state (e.g., from new state investments in tobacco prevention or increased statetobacco tax rates). These estimates can also be switched around to show what harms and costs Ohio would suffer from each one percentage point increase to its smoking rates or from each one percentage point reduction the State fails to obtain (e.g., because it fails to sustain adequate state tobacco prevention funding or lets its tobacco tax rates erode over time).

Fewer Smokers

Fewer current adult smokers: 87,000

Fewer current pregnant smokers: 1,500

Fewer current high school smokers: 6,500

Ohio kids alive today who will not become addicted adult smokers: 27,700

Public Health Benefits

Today's adults saved from dying prematurely from smoking: 23,100

Today's high school smokers saved from dying prematurely from smoking: 2,100

Ohio kids alive today who will not die prematurely from smoking: 8,900

	<u>First Year</u>	<u>Over 5 Years</u>
<i>Fewer smoking-affected births:</i>	1,500	7,450
<i>Fewer smoking-caused heart attacks:</i>	50	646
<i>Fewer smoking-caused strokes:</i>	29	347

[The number of heart attacks and strokes prevented each year by a one-time decline in adult smoking rates of one percentage point starts out small but grows sharply until it peaks and stabilizes after about ten years.]

Monetary Benefits (Reduced Public, Private, and Individual Smoking-Caused Costs)

	<u>First Year</u>	<u>Over 5 Years</u>
<i>Savings from smoking-affected birth reductions</i>	\$2.5 million	\$12.7 million
<i>Savings from heart attack & stroke reductions</i>	\$3.4 million	\$46.1 million

[Annual savings from fewer smoking-caused heart attacks and strokes grows substantially each year as more and more are prevented by the initial one percentage point smoking decline. Savings from prevented smoking-caused cancer are even larger, but do not begin to accrue until several years after the initial smoking decline.]

Reduction to future health costs from adult smoking declines: \$826.5 million

Reduction to future health costs from youth smoking declines: \$484.8 million

[These savings accrue over the lifetimes of the adults who quit and the youth who do not become adult smokers. Roughly 17.7% of smoking-caused healthcare expenditures in Ohio are paid by its Medicaid program.]

At the same time that they reduce public and private smoking-caused costs, state smoking declines also increase public and private sector worker productivity and strengthen the state's economy.

APPENDIX D

EXPLANATIONS AND SOURCES FOR TFK'S PROJECTIONS OF NEW REVENUES & BENEFITS FROM STATE CIGARETTE TAX INCREASES

The Campaign for Tobacco-Free Kids (TFK) projections of increased state revenues and other benefits from raising state cigarette tax rates reflect the basic fact that cigarette tax increases both boost state cigarette tax revenues and reduce smoking because the increased tax per pack brings in more new revenue than is lost from the declines in pack sales caused by consumption declines or increased smoker tax avoidance prompted by the price increase.

These projections are based, in part, on research findings that a 10% cigarette price increase, if maintained against inflation, reduces youth smoking rates by 6.5% or more, adult rates by 2%, and total consumption by 4%. [See, e.g., Chaloupka, FJ, "Macro-Social Influences: The Effects of Prices and Tobacco Control Policies on the Demand for Tobacco Products," *Nicotine & Tobacco Research*, 2000, and other price studies at <http://tigger.uic.edu/~fjc>; Tauras, J, et al., "Effects of Price and Access Laws on Teenage Smoking Initiation: A National Longitudinal Analysis," Bridging the Gap Research, ImpacTeen, April 24, 2001, and other price studies at <http://www.impactteen.org>.] But these elasticity findings are adjusted downward to be conservative and to account for some smokers avoiding the price increases through a range of tax evasion strategies. Despite such tax evasion, cigarette tax increases reduce smoking rates, which, in turn, reduces smoking caused disease, death, and economic costs. Parallel increases to state excise taxes on other tobacco products would similarly provide additional new state excise tax and sale tax revenue – while also reducing the use of these products in the state, and reducing related harms and healthcare costs.

These projections are fiscally conservative because they include generous adjustments for lost state pack sales (and reduced state revenue gains) caused by new tax avoidance efforts by continuing in-state smokers and, where applicable, fewer in-state cigarette sales to supply smokers from other states, informal smugglers, criminal smuggling organizations, or multistate internet sellers. [See, e.g., Farrelly, M, et al., "Cigarette Smuggling Revisited," U.S. Centers for Disease Control & Prevention (CDC), in press, and Farrelly, M, et al., *State Cigarette Excise Taxes: Implications for Revenue and Tax Evasion*, RTI International, 2003, http://www.rti.org/pubs/8742_Excise_Taxes_FR_5-03.pdf.] To account for possible additional declines in state cigarette sales and revenues from other factors – such as state tobacco prevention investments, other public and private tobacco prevention efforts, federal cigarette tax changes, cigarette company or other increases to cigarette prices, etc. – these projections also assume a background year-to-year decline in consumption of 1.5%. To be even more conservative, the projected amounts have also been rounded down.

Despite all of these conservative adjustments, the projections still show that non-trivial state cigarette tax increases will both significantly reduce smoking levels and substantially increase state revenues. The increased tax per pack will still bring in more new state revenue than is lost from the decrease in the number of packs sold caused by the tax increase from either consumption declines, tax avoidance, or smuggling. And that is exactly what has happened in every state that has significantly increased its cigarette tax rates. [See, e.g., TFK Factsheet, *Raising State Cigarette Taxes Always Increases State Revenues (and Always Reduces Smoking)*, <http://tobaccofreekids.org/research/factsheets/pdf/0098.pdf>.]

In those states that apply their sales tax percentage to the total retail price of a pack of cigarettes (including the state cigarette tax amount), a cigarette tax increase will raise state sales tax revenues per pack, which will offset sales tax revenue losses from fewer packs being sold. In addition, smokers who quit or cut back will likely spend the money they previously spent on cigarettes largely on other goods on which sales tax is collected, which further increases state sales tax revenues.

These projections assume that the tax increase is fully passed on in higher prices, and keeps up with inflation over time. The starting price per pack (before the proposed cigarette tax increase) used in these projections includes all federal and statewide excise and sales taxes but not any purely local taxes (except that NY City's \$1.50 per pack tax is factored into the overall NY State price per pack), and is based on data from *The Tax Burden on Tobacco*, 2007, reports of state cigarette tax increases, and media reports on tobacco company price changes, USDA Economic Research Service, Tobacco Briefing Room. The starting price per pack data

* Cigarette company price cuts and other factors could also work to increase cigarette consumption and/or sales in the state, which would increase state cigarette tax revenues beyond the projected amounts.

have been slightly adjusted downward because *The Tax Burden on Tobacco* does not completely account for retailer-based discounts, promotions, and coupons.

These projections assume that the state or district will follow standard practice and apply the cigarette tax increase to all previously tax-stamped or otherwise tax-paid cigarettes held in inventory by wholesalers or retailers on the effective date of the increase. Failing to tax such cigarettes held in inventory would open the door to massive pre-increase stockpiling by retailers and wholesalers to evade the increase, drastically reducing the amount of new state revenues.

The projections for youths stopped from becoming smokers and avoided premature youth and adult deaths are calculated by applying the above findings regarding the effects of tax and price increases to the number of current adult smokers in each state and to estimates from CDC of the number of kids alive today in each state who will become adult smokers and the number projected to die from smoking. [CDC, *State Data Highlights 2006*.] For an explanation of how CDC makes these youth projections, see CDC, "Projected Smoking-Related Deaths Among Youth – United States," *MMWR* 45(44):971-974, November 11, 1996, which also contains data on relative death risks of smokers, nonsmokers, former smokers, etc.]

Because of research and data limitations, it is not yet possible to estimate health savings in each year following a cigarette tax increase, or even provide reasonable estimates of the total health care savings over the first five or ten years. Although smoking-caused healthcare cost savings from a cigarette tax increase will be relatively small in the first year after an increase, they grow quickly. The listed 5-Year savings from fewer smoking-caused heart attacks and strokes and from fewer smoking-affected pregnancies and related birth complications show just some of the many substantial savings from the smoking reductions prompted by a tax increase that begin to accrue immediately.

The projected healthcare savings from reducing the number of future youth and current adult smokers accrue over the lifetimes of kids alive in the state today who quit or don't start because of tax increase and over the lifetimes of those current adult smokers who quit because of the tax increase. Smokers' lifetime healthcare costs average at least \$16,000 higher than nonsmokers (in 2002 dollars), despite shorter life spans; but the savings per each adult quitter are less than that because adult smokers have already been significantly harmed by their smoking and have already incurred or locked-in extra, smoking-caused health costs. [Hodgson, TA, "Cigarette Smoking and Lifetime Medical Expenditures," *The Millbank Quarterly* 70(1), 1992. See also, Nusselder, W, et al., "Smoking and the Compression of Morbidity," *Epidemiology & Community Health*, 2000; Warner, K, et al., "Medical Costs of Smoking in the United States: Estimates, Their Validity, and Their Implications," *Tobacco Control* 8(3):290-300, Autumn 1999. CDC, "Projected Smoking-Related Deaths Among Youth – United States," *MMWR* 45(44):971-974, November 8, 1996. See also, "Annual Smoking-Attributable Mortality, Years of Potential Life Lost, and Economic Costs – United States 1995-1999," *MMWR* 51(14):300-303, April 11, 2002.]

5-Year Heart & Stroke Savings projections show the estimated reductions in smoking-caused healthcare expenditures within first five years after the tax increase from reduced smoking-caused heart attacks and strokes, based on Lightwood & Glantz, "Short-Term Economic and Health Benefits of Smoking Cessation – Myocardial Infarction and Stroke," *Circulation* 96(4), August 19, 1997. These savings will increase steadily in subsequent years. The projected 5-Year Smoking Births Savings accrue from declines in smoking among pregnant women and corresponding reductions in smoking-caused birth complications and related first-year health costs. [Miller, D, et al., "Birth and First-Year Costs for Mothers and Infants Attributable to Maternal Smoking," *Nicotine & Tobacco Research* 3:25-35, 2001; and state pregnancy-smoking and births data.]

All projected savings have been adjusted to 2002 dollars using the same methodology used by CDC to update its data on state smoking-caused costs. The projected savings amounts would be larger if put in 2004 dollars, but using CDC methodology to put them in 2002 dollars makes the projections more conservative and reliable and makes them comparable to CDC's estimates of smoking-caused state costs. [See CDC, *Sustaining State Programs for Tobacco Control: Data Highlights 2006*.] These projections do not include a range of additional short and long-term savings from other declines in smoking-caused health problems and other smoking-caused costs. [See, e.g., U.S. Department of the Treasury, *The Economic Costs of Smoking in the U.S. and the Benefits of Comprehensive Tobacco Legislation*, 1998.]

APPENDIX E

MAXIMIZING TOBACCO TAX REVENUE BENEFITS BY MINIMIZING SMUGGLING AND TAX EVASION

A 75-cent increase to Ohio's cigarette tax is not likely to spark substantial amounts of new cigarette smuggling in the state (there are much more profitable markets for smugglers in the other higher-tax states and cities), and increased tax evasion by continuing Ohio smokers would likely be marginal given smokers' preference for convenient purchases by the single pack. To minimize any tax evasion and smuggling, however, the state could take a number of relatively simple and inexpensive measures – thereby bringing in even more new revenues from the cigarette tax increase than projected.^{*}

By reducing cigarette smuggling, establishing a new high-tech state tax stamp would increase the already substantial amount of new revenues the state would receive from its cigarette tax increase. For instance, California, the only state with high-tech tax stamps, enjoyed a \$100 million increase in cigarette tax revenues in the first 20 months after the new tax stamps were introduced in 2005.²⁹ Taking advantage of new technologies of high-tech tax stamps can even better ensure that Ohio maintains its high revenues and does not aid in cigarette smuggling.[†]

Simply establishing a hotline for reporting illegal smuggling activity or contraband sales can be quite productive – especially if all retailers, distributors, and manufacturers are required to post the hotline number prominently in all their business locations. Similarly, relatively small increases in state enforcement resources directed at reducing illegal sales of contraband cigarettes by otherwise legally operating retailers could, for example, pay for themselves just in the fines and penalties they generate. This would simultaneously reduce the amount of state tax revenues lost to such contraband sales (both directly and by putting other retailers on notice that such contraband sales will be uncovered and prosecuted).

Another productive step would be to pass a strong new law, as many other states have done, to prohibit or restrict Internet and other mail-order sales of cigarettes and other tobacco products to state residents.[‡] Such sales are typically made with no payment at all of state taxes (and with no protections against sales to kids), and Internet cigarette sales have been growing steadily in recent years, with corresponding reductions to state cigarette tax revenues.[§] A tough new state law, however, would make it more difficult for state smokers to shift to Internet purchases after any new cigarette tax increase goes into effect – especially given the states attorneys' general new agreement with the credit card companies and common carriers. Under that agreement, Ohio's Attorney General may notify the credit card companies and common carriers about any Internet vendors making sales to smokers in violation of either federal or state law (which is another reason why the state should pass its own Internet tobacco law), and the credit card companies will take away those vendors' credit card rights and the common carriers will refuse to make any deliveries for the illegal Internet sellers.³⁰ Without the ability to accept payment by credit card or deliver by common carrier, those Internet vendors will find it difficult, if not impossible, to stay in business – and that method of smoker tax evasion will be much harder to employ.

^{*} To be conservative, the formulas used in this report to project the new state revenue amounts from the different cigarette tax increase amounts assume a significant amount of new cigarette smuggling and other smoker tax evasion efforts after the increases go into effect. See Appendix D. If the new smuggling and tax evasion assumed in these formulas does not occur or occurs to a lesser extent, the state would obtain even more new annual revenues than projected in this report. Appendix E lists the many steps the state could take to minimize such smuggling and tax evasion and maximize new revenues.

[†] For more information on high-tech tax stamps, see TFK Factsheet, *The Case for High-Tech Cigarette Tax Stamps*, <http://www.tobaccofreekids.org/research/factsheets/pdf/0287.pdf>.

[‡] For model legislation and additional information, see TFK website at <http://tobaccofreekids.org/research/factsheets/index.php?CategoryID=29>. For examples of other state laws and legislation to prohibit or restrict Internet tobacco product sales, see TFK website at <http://tobaccofreekids.org/reports/internet/resources.php#4>.

[§] See, e.g., TFK Factsheet, *Internet Sales of Tobacco Products: Reaching Kids & Evading Taxes*, <http://tobaccofreekids.org/research/factsheets/pdf/0213.pdf>.

A strong new state Internet tobacco sales law would not only provide Ohio with a more direct way to take advantage of the new agreement with the credit card companies and common carriers, but could also put other obstacles in the way of illegal Internet sellers efforts to sell contraband cigarettes to Ohio smokers.

There are many other cost-effective steps Ohio could take to further curtail tobacco tax evasion and cigarette smuggling – thereby increasing the total amount of net new tobacco tax revenues it would obtain from a tobacco tax increase. But even without these additional measures, a 75-cent cigarette tax increase with an increase in the OTP tax to match would bring the state new annual revenues of more than \$390.8 million.

STATE OPTIONS TO PREVENT AND REDUCE CIGARETTE SMUGGLING AND BLOCK OTHER ILLEGAL STATE TOBACCO TAX EVASION

To try to block or reduce state tobacco tax increases, the major U.S. cigarette companies regularly overstate the amount of cigarette smuggling and tax-avoidance prompted by differences among different states' cigarette tax rates. In fact, every state that has increased its cigarette tax rate significantly has enjoyed substantial revenue increases despite declining smoking levels and pack sales.¹ At the same time, recent research indicates that the highest- tax states could increase their tobacco tax revenues by five or 10 percent if they implemented effective measures to reduce sharply both organized cigarette smuggling (which accounts for the majority of untaxed sales) and smoker tax avoidance.² New revenue aside, states should not tolerate illegal tobacco smuggling or any other tobacco-related crimes, especially if done by criminal organizations. Fortunately, there are a number of relatively simple and inexpensive measures that states could implement to minimize such smuggling and tobacco tax avoidance.¹

Measures to Make Smuggling & Tobacco Tax Avoidance More Difficult[†]

1. ***Improve state tobacco tax stamps.*** The few states that do not have tax stamps (NC, SC, and ND) should require them; and all states should take advantage of available new technologies to make their tax stamps larger, highly visible, easy to distinguish from other states' tax stamps, harder to counterfeit, and placed on two sides of the packages and under any cellophane wrapper – with the tax stamp coding providing information on each pack re what retailer or wholesaler originally purchased it from which distributor or manufacturer. California, for example, initiated new high-tech tax stamps and enjoyed a \$120 million boost to its cigarette tax revenues in the following 20 months.³ Tax stamps on non-cigarette tobacco products should also be established or improved. Tax stamps could also provide a phone number or email address for reporting suspected illegal sales, smuggling, or tax evasion, with rewards for tips that lead to arrests (and new stamps could also include a quitline phone number for smokers who want to quit).

^{*} A recent U.S. Supreme Court ruling found that certain parts of Maine's law restricting Internet sales of tobacco products relating to common carriers were preempted by federal law regulating common carriers (*Rowe v. New Hampshire Motor Transport Assoc.*, February 20, 2008). But that ruling still leaves the states free to prohibit all Internet or other mail order sales of tobacco products and to prohibit all related deliveries. In addition, the states may still place substantial restrictions and requirements on the Internet and mail-order sellers, themselves – but may not place any direct or indirect requirements or restrictions on common carriers (other than a complete prohibition on certain, or all, cigarette deliveries). See TFK Factsheets, *Model State Legislation to Restrict Internet & Mail-Order Tobacco Products Sales*, <http://www.tobaccofreekids.org/research/factsheets/pdf/0230.pdf>, and *The Critical Importance of a Delivery-List Enforcement Provision in State Internet Tobacco Sales Legislation*, <http://www.tobaccofreekids.org/research/factsheets/pdf/0259.pdf>.

[†] U.S. interstate cigarette smuggling typically occurs when smugglers purchase cigarettes in a low-tax state or other low-tax or no-tax jurisdiction (such as Indian Tribal lands) and then illegally smuggle them into a high-tax state for illegal resale to otherwise-legal retailers. Otherwise legal retailers then purchase the cigarettes from the smugglers at prices that reflect the avoided state cigarette taxes, and the retailers subsequently sell the cigarettes to unknowing consumers. Through this process, the retailers and the smugglers, and not the smokers, enjoy the lion's share of the tax-avoidance "savings." In some cases, the cigarettes smuggled from the low-tax jurisdiction are sold directly to final customers via black-market sales, but these black-market sales are quite small compared to the sales through otherwise legal retailers. Some smokers also avoid paying the cigarette tax in their state by purchasing their cigarettes in a nearby lower-tax state, from stores on nearby military bases or Indian Lands (which typically do not charge state taxes), or from the Internet (where sales of cigarettes from Tribal lands and low-tax states are common).

[‡] Although many of these measures refer only to cigarettes, they could be applied to other tobacco products, as well.

2. **Require State tax-exempt stamps on all cigarettes and other tobacco products sold in state that are not subject to the state's tobacco taxes.** Require distributors selling cigarettes to Indian Tribes and others that make legal cigarette sales within the state's borders free from state tax to stamp those cigarettes with special state tax-exempt stamps – and to report all such sales, including amounts sold to whom, to state tax collection officials. The stamps could state “for legal tax-exempt sales only.” These stamps would make it more difficult to illegally divert tax-exempt cigarettes into non-tax-exempt sales and would provide state officials with important data on the extent of tax-exempt sales and illegal diversion within the state. Several states already have such tax-exempt stamping requirements.⁴
3. **Forbid the sale, purchase, or possession in the state of any tobacco products that are not marked with state tobacco tax stamps or other state tax-payment indicia establishing that all applicable state tobacco taxes have already been paid – other than small personal-use amounts and those held by or transported between licensed cigarette manufacturers, distributor/wholesalers, retailers or other licensed tobacco product businesses.** This catch-all requirement prohibits all sorts of cigarette smuggling and tax avoidance, mandates tax payments, and facilitates enforcement by establishing that any significant amount of tobacco products found in the state without the appropriate tax stamp or tax-payment indicia are illegal goods (unless in the possession of licensed tobacco product businesses or their delivery services).
4. **Require better record keeping by distributor/wholesalers.** Require distributors and wholesalers selling cigarettes to retailers (which, in turn, sell them to state residents) to keep and maintain records of amounts sold, to whom, tax-stamp status, etc., and to regularly provide this information to state officials.
5. **Require better record keeping by retailers.** Require all retailers that sell cigarettes in the state to keep and retain accurate records regarding: a) their receipt of cigarettes from others (including date, quantity, from whom received, etc.); b) their total cigarette sales in the state (with monthly totals); and c) their sale of any cigarettes in quantities exceeding 2,000 cigarettes, or 10 cartons (including date, quantity, description, to whom sold, etc.).
6. **Block retail sales clearly not for personal use.** Place a maximum sale amount of 2,000 cigarettes (10 cartons) for any single sale to a consumer in the state – with parallel limits for the sales of other tobacco products.
7. **Educate smokers about existing state laws restricting smuggling and tax avoidance.** Most states already have laws that prohibit state smokers from bringing more than two cartons of cigarettes (or some other maximum amount) into the state from any other jurisdiction (including nearby states, Tribal lands, military bases, and duty-free shops) – and states that do not have any such laws should pass them. While enforcing such laws is difficult, many smokers do not even know they exist – and some would stop going to other jurisdictions to buy cheaper cigarettes (or at least reduce the size of their purchases) if they did know about these laws. Similarly, many smokers do not know that it is against state law to avoid paying state cigarette taxes by purchasing them over the Internet from website sellers that do not collect or pay the tax owed to the state. To educate smokers about existing laws prohibiting tax avoidance the State could post the information on various state website pages, issue related press releases, run related public education announcements, and require retailers to post notices or include notices with each tobacco product sale they make. Making periodic highly publicized “stings” to catch some of the cross-border or Internet shoppers who are illegally evading the state cigarette tax might be an even more effective way to dampen many smokers’ enthusiasm for these tax avoidance strategies.
8. **Publicize toll-free hot lines to encourage reports of smuggling or tax-avoidance activities.** Require state-based wholesalers, distributors, importers, exporters, and retailers of tobacco products to post prominent signs that provide a toll-free number and email address for reporting anyone suspected of smuggling tobacco products or buying or selling smuggled tobacco products. These or other signs could also provide information on how to identify legal versus smuggled cigarettes, notify smokers and others of the existing laws and penalties re buying smuggled cigarettes, bringing cigarettes into the state from other jurisdictions, etc., and inform employees of existing whistleblower protections. The toll-free number could also be included on the state tax stamps placed on tobacco products.

9. **Protect “Whistleblowers.”** To encourage the reporting of smuggling activities and protect witnesses, states could pass laws to protect the employees of retailers, distributors, wholesalers, importers, exporters, manufacturers, and delivery services from being fired or otherwise penalized by their employers if the employee notifies authorities about their employers’ smuggling-related wrongdoing or testifies about it in court.
10. **Work with Neighboring States.** To increase each state’s cigarette tax revenues, groups of neighboring states can work together to make their cigarette tax rates equal or similar to each other’s (by the lower-tax states raising their rates) and can coordinate and expand their mutual efforts to minimize cigarette smuggling and other tax avoidance through new parallel state laws and coordinated enforcement efforts.
11. **Put pressure on the States with extremely low cigarette tax rates to raise them.** The average state cigarette tax is more than 107 cents per pack, but many states have rates way below that average. Cigarette tax increases in those states would help to dampen interstate cigarette smuggling by sharply reducing the available illegal profits. Similarly, very few Indian Tribes have their own Tribal tobacco taxes, and they should be encouraged to establish them (see the next item). States and Tribes with low or no taxes on other tobacco products should also be urged to establish or raise them.
12. **Enter into treaties with in-state Indian Tribes to eliminate tobacco product price disparities.** Some smokers and smugglers go onto Tribal lands to purchase cigarettes and other tobacco products free of any state taxes. To reduce this problem, some states have entered into special compacts or agreements with the Indian Tribes located within the states’ borders whereby the Tribe agrees to collect the state’s tax (or a similar Tribal tax) on all of cigarette or other tobacco product sales on the Tribe’s lands (whether sold to Tribal members or nonmembers) – thereby making the Tribal prices comparable to the prices charged elsewhere in the state – and the state agrees that the Tribe can keep all of the revenues it raises from charging the state (or Tribal) tax. These kinds of state-Tribal agreements are necessary because, otherwise, when a Tribe establishes a Tribal cigarette tax it is legally required to collect that Tribal tax on top of any state cigarette tax in all sales to non-tribal members, which produces an odd double-taxation problem.⁵
13. **Support Federal Anti-Smuggling Legislation.** While each state can do a lot, the federal government can do more. Most notably, the federal government could require all states to put tax stamps on their cigarettes, thereby stopping the sale in some low-tax states of blank packs that can easily be used for smuggling – and could require special tax stamps or restricted-sale notices on all tobacco products sold free of state taxes on Indian reservations, military bases, and duty-free shops. The federal government can also create nationwide standards for tax stamps; cigarette labeling (e.g., requiring unique serial numbers or markings indicating where packs may be legally sold); record keeping by manufacturers, wholesalers, and retailers; maximum sales amounts; and the like.⁶ Federal legislation could also block tax-avoidance via Internet sales (see below).

Special Measures to Stop Illegal Tax-Free Internet & Mail Order Sales of Cigarettes

The federal Jenkins Act requires all Internet sellers to provide each state with monthly reports listing state residents who have purchased cigarettes from the Internet sellers (including the quantities sold to each and the residents’ mailing addresses), thereby enabling states to go after the in-state consumers to collect state taxes owed on the sales. The vast majority of Internet sellers, however, do not make the required Jenkins Act reports to the states, and federal officials rarely enforce the Act.⁷ Some states have marginally increased the Internet sellers’ compliance rate simply by contacting them and demanding the reports, and a few states have initiated lawsuits against some Internet sellers to try to force compliance, but overall compliance rates remain low. While these state efforts could be expanded, they are ultimately of limited value given the large number of Internet sellers and the ability of customers to find new non-complying vendors quickly and easily on the Internet. Even when Internet vendors comply with the Jenkins Act and provide the states with the customer information, going after each individual customer to

⁵ Retailers on Indian Lands are allowed to sell tobacco products to members of the same Tribe free of state tobacco taxes but are not allowed (unless expressly authorized by a state) to sell state-tax-free cigarettes to anyone who is not a Tribal member. However, a state’s ability to take enforcement action against Indian Tribes that fail to collect and remit state taxes on sales to non-members of the Tribe are severely limited because of Indian Tribes’ sovereign immunity (e.g., states cannot bring Tribes into state court to enforce state tax collection laws).

collect owed taxes is an inevitably time consuming and ineffective process. Accordingly, states that wish to minimize Internet-based tobacco tax evasion must go beyond trying to enforce the Jenkins Act and also establish more effective tax collection strategies.

- **Implement new State laws banning or restricting Internet tobacco product sales.** New York State has a law in place that prohibits Internet or mail order sales of cigarettes into the state – and the courts have upheld that law against cigarette company and Internet vendor attacks.⁸ To minimize Internet sales that avoid paying state taxes, a state could pass a ban similar to the New York law.⁹ Alternatively, a state could establish laws – such as those in Maine, California, Texas and other states – placing new requirements on all Internet and mail-order sales of any tobacco products to any state residents.¹⁰ To be effective, any such law must provide some way of interrupting illegal Internet sales without the state having to try to find and bring every one of the hundreds of active illegal internet sellers into court. The best way to do that is to block the illegal Internet sellers' deliveries to their customers in the state by instructing common carriers and other delivery services operating in the state not to make any deliveries for Internet sellers that are breaking state laws.¹¹
- **Support new federal laws to minimize Internet-based tobacco tax evasion.** As with smuggling in general, new federal laws can more effectively restrict Internet-based tobacco tax evasion than state laws because the federal government has nationwide authority, can restrict interstate commerce in ways that states cannot, and can restrict U.S. Postal Service deliveries of illegally sold or contraband tobacco products. One effective federal bill to reduce tobacco tax evasion by restricting Internet tobacco product sales and strengthening other federal laws against contraband tobacco products was the Prevent All Contraband Tobacco Act, known as the PACT Act (S. 1117), which passed the Senate in the 2003-2004 legislative session but was not considered in the House.¹² New versions of the PACT Act will be introduced in both the House and Senate this session.
- **Subject Internet and other mail-order sellers of tobacco products to the same anti-smuggling measures and other state laws that apply to regular in-state retailers of tobacco products.** To create a more level playing field and reduce the unfair cost and price advantage of Internet tobacco product sellers (which underlies Internet-based tax evasion), make sure all anti-smuggling provisions and other state laws that apply to in-state retail sellers of tobacco products also apply to Internet or mail-order companies that sell tobacco products to persons in the state, including record-keeping requirements, applicable penalties, etc., with adjustments made to the requirements placed on in-state retailers, as necessary, to apply them in ways that account for the unique character of Internet sales.

Stronger Disincentives and Punishments for Smuggling

- **Expand definition of illegal smuggling subject to state prosecution and penalties.** To reach more illegal smuggling and tax avoidance through state law enforcement, reduce the minimum number of cartons/packs/cigarettes that trigger smuggling violations or major smuggling penalties. Establish or fortify penalties for the manufacture, possession, or sale of counterfeit tobacco tax stamps or counterfeit tobacco products.
- **Increase existing fines for cigarette or other tobacco product smuggling.** Increase the minimum dollar amounts of existing fines and have no maximum amount so that meaningful fines can be levied against large economic entities involved in smuggling.
- **Seize vehicles and properties used in cigarette or other tobacco product smuggling.** Establish new provisions to allow for the state's seizure of vehicles used in cigarette smuggling, putting liens on property for the value of smuggled goods, etc. (as with state laws pertaining to illegal drug trafficking).
- **Withdraw right to sell tobacco products from retailers involved in smuggling.** State anti-smuggling laws could ensure that retail outlets in the state that buy smuggled cigarettes or knowingly sell smuggled cigarettes will lose their right to sell any cigarettes in the state for some period of time (e.g., from one to ten years depending on the severity of the violation).
- **Include jail or prison time for guilty large-scale smugglers or repeat offenders.** Going beyond just fines and other economic disincentives, state laws could call for jail or prison sentences for persons participating in large smuggling efforts or who are guilty of repeatedly violating the states anti-smuggling or tax-avoidance laws.

Endnotes for Appendix E

¹ Farrelly, M, et al., *State Cigarette Excise Taxes: Implications for Revenue and Tax Evasion*, Research Triangle International, May 2003, http://www.rti.org/pubs/8742_Excise_Taxes_FR_5-03.pdf. See also, Campaign for Tobacco-Free Kids (TFK), *Raising State Tobacco Taxes Always Increases State Revenues & Always Reduces Tobacco Use*, <http://tobaccofreekids.org/research/factsheets/pdf/0098.pdf>.

² Yurekli, A & Zhang, P, "The Impact of Clean Indoor-Air Laws and Cigarette Smuggling on Demand for Cigarettes: An Empirical Model," *Health Economics* 9:159-170, 2000; Farrelly, M, et al., "Cigarette Smuggling Revisited," U.S. Centers for Disease Control & Prevention (CDC), in press. See also, the references listed in endnote 1.

³ Halper, E, "States Tobacco Revenue Surges," *Los Angeles Times*, December 27, 2005. TFK Factsheet, *The Case for High-Tech Cigarette Tax Stamps*, <http://tobaccofreekids.org/research/factsheets/pdf/0287.pdf>. California Revenue and Taxation Code Section 30162, <http://www.leginfo.ca.gov/cgi-bin/displaycode?section=rtc&group=30001-31000&file=30161-30165>. For the underlying legislation, see http://www.leginfo.ca.gov/pub/01-02/bill/sen/sb_1701-1750/sb_1701_bill_20020926_chaptered.pdf.

⁴ See, e.g., Arizona's separate tobacco tax, with tax stamps, on Tribal sales, with the revenues remitted to the Tribes. AZ Revised Statutes, 42-3301 to 42-3307, <http://www.azleg.state.az.us/ars/42/title42.htm>.

⁵ See above note re: AZ. For examples of State-Tribal tobacco tax compacts, National Congress of American Indians, http://www.ncai.org/main/pages/issues/governance/agreements/tax_agreements.asp.

⁶ For a list of effective federal anti-smuggling provisions, see American Cancer Society, et al., *Proposed Federal Measures to Reduce Cigarette Smuggling and Protect Federal and State Tobacco Tax Revenues*, January 2003, <http://tobaccofreekids.org/research/factsheets/pdf/0226.pdf>.

⁷ See, e.g., U.S. General Accounting Office, *Internet Cigarette Sales: Giving ATF Investigative Authority May Improve Reporting and Enforcement*, August 9, 2002, <http://www.gao.gov/new.items/d02743.pdf>.

⁸ New York Public Health Article 13F, Section 1399-II, <http://assembly.state.ny.us/leg/?cl=91&a=71>. *Brown & Williamson Tobacco Corp. v. Pataki*, U.S. Court of Appeals for the Second Circuit, Docket Nos. 01-7806, 01-7813, February 13, 2003, <http://tobacco.neu.edu/Internet/CCA2ruling.pdf>.

⁹ For model legislation, see <http://tobaccofreekids.org/research/factsheets/index.php?CategoryID=29>.

¹⁰ For model legislation, see <http://tobaccofreekids.org/research/factsheets/pdf/0230.pdf>.

¹¹ For more information on blocking Internet deliveries, see the provisions in the above cited model statutes and the TFK Factsheet at <http://tobaccofreekids.org/research/factsheets/pdf/0259.pdf>. More on how to address Internet tobacco product sale is at <http://tobaccofreekids.org/reports/Internet> and <http://tobaccofreekids.org/research/factsheets/index.php?CategoryID=29>.

¹² For more information on the PACT Act, see <http://tobaccofreekids.org/reports/Internet>.

USEFUL RESEARCH STUDIES

Tobacco Tax, Price, and Consumption

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