



March 12, 2015

Chairman Mark Hass  
Vice Chair Brian Boquist  
Senator Herman Baertschiger, Jr.  
Senator Chris Edwards  
Senator Chuck Riley

Senate Finance and Revenue Committee  
900 Court St. NE, S-213  
Salem, OR 97301

Dear Chairman Hass, Vice-Chair Boquist and Committee Members:

Core-Mark International, Inc., Portland Division is a broad line distributor of supplies and services to the convenience retail industry. In this capacity we employ approximately 200 Oregonians and also manage our Grants Pass distribution center which employs approximately 100 Oregonians. Aggregately, the two distribution centers supply approximately 950 convenience stores. In 2014 the two divisions collected over \$74 million in cigarette stamp tax and another \$23 million in tobacco and cigar taxes for the state of Oregon. This \$97 million of the total \$258 million of revenue represents 38% of the total revenue collected.

As a responsible licensed distributor, Core Mark opposes Senate Bill 14 which changes Oregon's current law prohibiting Counties and municipalities from imposing a tobacco and cigarette tax in addition to Federal and in lieu of or addition to State excise taxes. With regard to cigarettes, SB 14 fails to designate whether or not a county tax stamp will or will not be attached to an individual cigarette package which could inherently create a lack of enforcement from the counties and in turn create an environment that would diminish taxable revenue collection. Nor does SB 14 address jurisdiction identification on tobacco and cigar products that currently are not subject to a tax stamp and are packaged by the manufacturer in a way that makes stamping cost prohibitive and ineffective.



1. **Higher tobacco taxes do not significantly reduce consumption, but rather higher taxes drive customers to seek lower priced goods and thus to avoid/evade taxes.**

The State of Oregon currently assesses a state tax of \$13.10 per carton while the State of Washington assesses a state tax of \$30.25 per carton. According to the recent Tax Foundation study, Washington has a 46.4% cigarette smuggling rate, and fails to collect excise taxes and sales tax on 113 million packs annually. Approximately 35 million of these packs are purchased in the state of Oregon. That leaves 78 million packs that were purchased primarily at tribal non-taxed reservations, other neighboring states, internet or black market.

The same phenomena will occur from county to county depending upon the rate of tax. Consumers are willing to drive miles to save costs and avoid higher taxation, as is evident with current Washington cross-border buying. County tax differentials therefore will cause tobacco customers to travel additional distances to save cost. Ancillary products purchased will also be lost as that customer is likely to reduce the number of stops in order to compensate for any additional mileage consumed and driving time. This will create an uneven playing field between competing counties.

Small format stores, mostly owned by independent business people, that are located on the border in a higher taxed county, will face direct competition from a competitor that resides in a lower taxed county. They will not be able to equitably compete. There are instances in the city of Portland where a convenience store located in Multnomah County competes with a large format grocery store located across the street in Clackamas County. They and similar others will literally be wiped out.

2. **The bill does not address the mechanics of identifying county jurisdiction.**

SB 14 does not designate whether or not individual county stamp taxes will be applied to each package of cigarettes in a carton. If indeed tax stamps are not required to be specific to a county jurisdiction, enforcement of the tax will be difficult if not impossible to impose. As a distributor, it has not been determined how certain cash & carry's, including COSTCO, would determine the rate at which they would pass the county tax to their customer base. Would the tax rate for a cash & carry be determined by the county within which they are located or by the county in which their customers reside? With the former, a cash & carry located in a high tax county would likely see a dramatic decline in sales and possibly choose to discontinue that category. This would further decrease the revenue expected by the county. In the case of the latter, this bill does not



address how proper identity would be determined for a customer to prove they should be charged the proper tax rate.

Legitimate law abiding wholesalers and distributors who have invested in information technology will be able to identify via county and assess the correct taxation amounts. Smugglers, who are not interested in the long term viability of their business or that of their customers, will gain a significant advantage to those who are doing business legally. Retailers and consumers, who are seeking the lowest possible cost of goods for competitive and economic reasons, will become easy prey to those who choose to avoid taxation. And unless the state and counties are willing to invest heavily in personnel whose sole purpose is enforcement of cigarette, cigar and tobacco tax conformity, legitimate distributors will face an unfair disadvantage which will significantly diminish sales and thereby tax collection for the state and counties.

**3. Multiple tax stamp jurisdictions create additional costs at the distribution level. These costs will get added to the end user which will further reduce consumption of in state product.**

If a stamp is assessed by county, the requirement to stamp multiple county jurisdictions will force distributors to stamp product on demand and by hand as opposed to the current system of machine pre-stamping product based upon daily state movement history. This will force production cost up at least three times that of what it costs at today's current rate. And while there are stamp machines that are capable of handling multiple jurisdictions (up to four jurisdictions), the lease amount is three times that of a single jurisdiction machine. These business costs must and will be passed to the retailer who in turn will pass the additional cost to the end consumer. This will create further incentive for the end user to shop for the lowest priced product, which could very well mean shopping out of state, via internet or black market. Inevitably, this will reduce tax revenues for the state and hurt the Oregon economy while creating a nightmare for legitimate tax abiding distributors.

Other Tobacco Products (OTP), which include chewing and pipe tobacco and cigars, currently do not require stamp identification. The product is packaged in a way that is not conducive to stamping and there is no machinery available that can separate the product from the package, apply a tax stamp then reseal. In order to apply a stamp the product would require individual selling units to be hand separated from the package, hand stamped and then hand banded together again for wholesale. As a consequence, wholesale costs would rise dramatically to cover the associated cost of labor. States who have attempted to apply a tax stamp in the past on chewing



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tobacco have met with resistance from manufactures who have stated that they will simply cease selling their product in those states rather than change their packaging for a single state.

In both cases, distributors are not equipped with machinery that can perform tax application in an effective low cost manner. If an individual county tax stamp is required wholesale/distributor costs will have to increase to cover the increased labor costs. Inevitably, this will reduce tax revenues for the state and hurt the Oregon economy while creating a nightmare for legitimate tax abiding distributors and wholesalers.

For the reasons above, we strongly oppose relinquishing the State's sole taxing authority on cigarettes and tobacco products to cities, counties or other municipal entities.

Respectfully submitted,



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Core-Mark International, Inc.

# Cigarette Taxes and Cigarette Smuggling by State, 2013

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## Key Findings

- Large differentials in cigarette taxes across states create incentives for black market sales.
- Smuggled cigarettes make up substantial portions of cigarette consumption in many states, and greater than 20 percent of consumption in fifteen states.
- The highest inbound cigarette smuggling rates are in New York (58.0 percent), Arizona (49.3 percent), Washington (46.4 percent), New Mexico (46.1 percent), and Rhode Island (32.0 percent).
- The highest outbound smuggling rates are in New Hampshire (28.6 percent), Idaho (24.2 percent), Virginia (22.6 percent), Delaware (22.6 percent), and Wyoming (21.0 percent).
- Smuggling rates jumped substantially in Illinois after hikes in state and county excise tax rates, from 1.1 percent of consumption in the last edition to 20.9 percent in this edition.
- Cigarette tax rates increased in 30 states and the District of Columbia between 2006 and 2013.

Public policies often have unintended consequences that outweigh their benefits. One consequence of high state cigarette tax rates has been increased smuggling as criminals procure discounted packs from low-tax states to sell in high-tax states. Growing cigarette tax differentials have made cigarette smuggling both a national problem and a lucrative criminal enterprise.

Each year, scholars at the Mackinac Center for Public Policy, a Michigan think tank, use a statistical analysis of available data to estimate smuggling rates for each state.<sup>1</sup> Their most recent report uses 2013 data and finds that smuggling rates generally rise in states after they adopt large cigarette tax increases. Smuggling rates have dropped in some states, however, often where neighboring states have higher cigarette tax rates. Table 1 shows the data for each state, comparing 2013 and 2006 smuggling rates and tax changes.

New York is the highest net importer of smuggled cigarettes, totaling 58.0 percent of the total cigarette market in the state. New York also has the highest state cigarette tax (\$4.35 per pack), not counting the additional local New York City cigarette tax (an additional \$1.50 per pack). Smuggling in New York has risen sharply since 2006 (+62 percent), as has the tax rate (+190 percent).

Smuggling in Illinois has also increased dramatically, from 1.1 percent to 20.9 percent since the last data release. This is likely related to the fact that the Illinois state cigarette tax rate was hiked from \$0.98 to \$1.98 in mid-2012. This increase in smuggling may continue in future data editions, as more recent increases in both the Cook County rate (from \$2.00 to \$3.00 per pack, effective March 1, 2013) and the Chicago municipal rate (from \$0.68 to \$1.18, effective January 10, 2014) have brought the combined state-county-municipal rate in the city of Chicago to \$6.16 per pack of cigarettes, the highest combined rate in the country.<sup>2</sup>

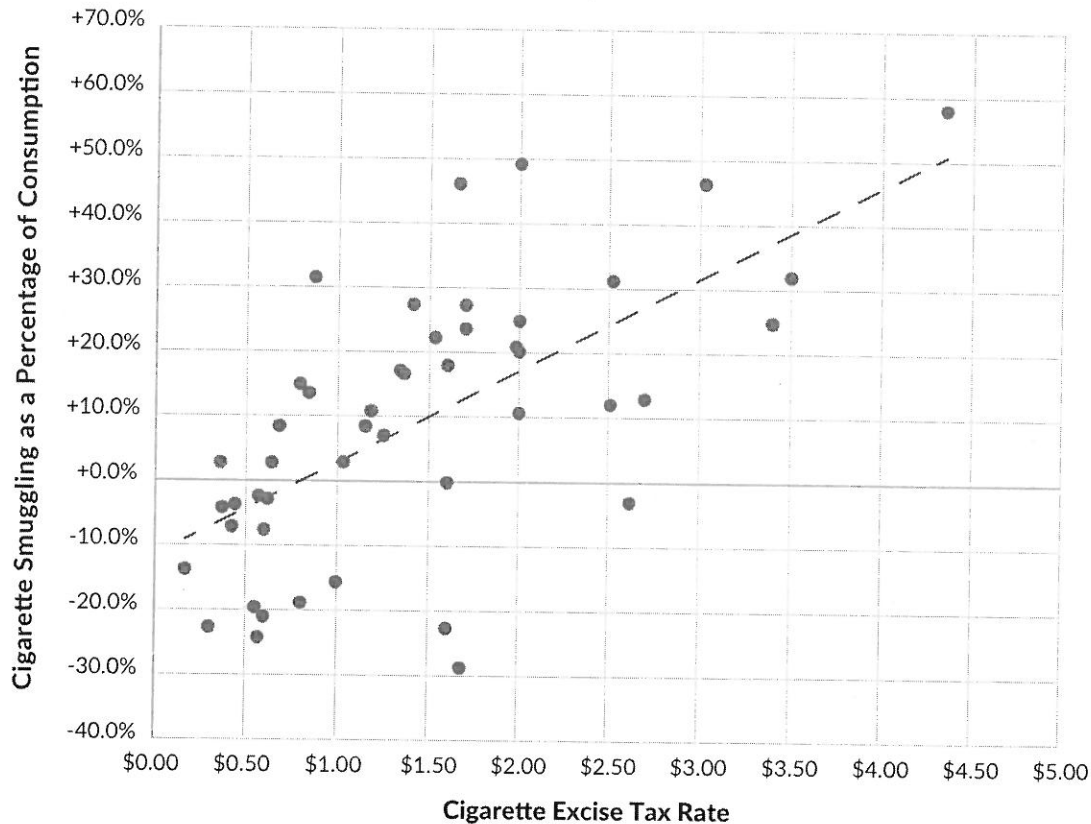
Other peer-reviewed studies provide support for these findings.<sup>3</sup> Recently, a study in Tobacco Control examined littered packs of cigarettes in five northeast cities, finding that 58.7 percent of packs did not have proper local stamps. The authors estimated 30.5 to 42.1 percent of packs were trafficked.<sup>4</sup>

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- 1 See, e.g., Mackinac Center for Public Policy, Michael LaFaive, Todd Nesbit, & Scott Drenkard, *Cigarette Smugglers Still Love New York and Michigan, but Illinois Closing In* (Feb. 2015), <http://www.mackinac.org/20900>; Mackinac Center for Public Policy, Michael LaFaive, & Todd Nesbit, *Cigarette Smuggling Still Rampant in Michigan, Nation* (Feb. 2014), <http://www.mackinac.org/19725>; Mackinac Center for Public Policy, Michael LaFaive, & Todd Nesbit, *Higher Cigarette Taxes Create Lucrative, Dangerous Black Market* (Jan. 2013), <http://www.mackinac.org/18128>; Mackinac Center for Public Policy, Michael LaFaive, *Cigarette Taxes and Smuggling 2010: An Update of Earlier Research* (Dec. 2010), <http://www.mackinac.org/14210>; Mackinac Center for Public Policy, Michael LaFaive, Patrick Fleenor, & Todd Nesbit, *Cigarette Taxes and Smuggling: A Statistical Analysis and Historical Review* (Dec. 2008), <http://www.mackinac.org/10005>.
  - 2 The Civic Federation, *Higher Tax Rates in Effect for Chicago Tobacco Consumers* (Jan. 2014), <http://www.civicfed.org/civic-federation/blog/higher-tax-rates-effect-chicago-tobacco-consumers>.
  - 3 See, e.g., Michael F. Lovenheim, *How Far to the Border?: The Extent and Impact of Cross-Border Casual Cigarette Smuggling*, *National Tax Journal*, Vol. LXI, No. 1, (March 2008), [http://ntj.tax.org/wwtax/ntjrec.nsf/BF515771548F9D538525742E006CCBBA/\\$FILE/Article%2001-Lovenheim.pdf](http://ntj.tax.org/wwtax/ntjrec.nsf/BF515771548F9D538525742E006CCBBA/$FILE/Article%2001-Lovenheim.pdf); R. Morris Coats, *A Note on Estimating Cross Border Effects of State Cigarette Taxes*, *National Tax Journal*, Vol. 48, No. 4, (December 1995), pp. 573-84, [http://ntj.tax.org/wwtax/ntjrec.nsf/notesview/D7AF38C6EF8BF6D7852567EF0057A8CO/\\$file/v48n4573.pdf](http://ntj.tax.org/wwtax/ntjrec.nsf/notesview/D7AF38C6EF8BF6D7852567EF0057A8CO/$file/v48n4573.pdf); Mark Stehr, *Cigarette Tax Avoidance and Evasion*, *Journal of Health Economics*, Vol. 24, (2005), pp. 277-97, <http://legacy.library.ucsf.edu/documentStore/h/j/o/hjo10j00/Shjo10j00.pdf>.
  - 4 Kevin C. Davis et. al., *Cigarette Trafficking in Five Northeastern US Cities*, *Tobacco Control*, December 2013, <http://tobaccocontrol.bmj.com/content/early/2013/12/11/tobaccocontrol-2013-051244>.

Smuggling takes many forms: counterfeit state tax stamps, counterfeit versions of legitimate brands, hijacked trucks, or officials turning a blind eye.<sup>5</sup> The study's authors, LaFaive and Nesbit, cite examples of a Maryland police officer running illicit cigarettes while on duty, a Virginia man hiring a contract killer over a cigarette smuggling dispute, and prison guards caught smuggling cigarettes into prisons. Policy responses have included banning common carrier delivery of cigarettes,<sup>6</sup> greater law enforcement activity on interstate roads,<sup>7</sup> differential tax rates near low-tax jurisdictions,<sup>8</sup> and cracking down on tribal reservations that sell tax-free cigarettes.<sup>9</sup> However, the underlying problem remains: high cigarette taxes that amount to a "price prohibition" of the product in many U.S. states.<sup>10</sup>

## Cigarette Smuggling Rises with Excise Tax Rates

Cigarette Smuggling vs. State Cigarette Excise Tax Rate, 2013



Note: Positive smuggling percentages are inflow to a state; negative percentages are outflow.  
Source: Mackinac Center for Public Policy; Tax Foundation.

- 5 See, e.g., Scott Drenkard, *Tobacco Taxation and Unintended Consequences: U.S. Senate Hearing on Tobacco Taxes Owed, Avoided, and Evaded*, TAX FOUNDATION, July 29, 2014, <http://taxfoundation.org/article/tobacco-taxation-and-unintended-consequences-us-senate-hearing-tobacco-taxes-owed-avoided-and-evaded>.
- 6 See, e.g., Curtis Dubay, *UPS Decision Unlikely to Stop Cigarette Smuggling*, TAX FOUNDATION TAX POLICY BLOG, Oct. 25, 2005, <http://taxfoundation.org/blog/ups-decision-unlikely-stop-cigarette-smuggling>.
- 7 See, e.g., Gary Fields, *States Go to War on Cigarette Smuggling*, WALL STREET JOURNAL, Jul. 20, 2009, <http://professional.wsj.com/article/SB124804682785163691.html?mg=reno64-wsj>.
- 8 See, e.g., Mark Robyn, *Border Zone Cigarette Taxation: Arkansas's Novel Solution to the Border Shopping Problem*, TAX FOUNDATION FISCAL FACT No. 168 (Apr. 9, 2009), <http://taxfoundation.org/article/border-zone-cigarette-taxation-arkansas-novel-solution-border-shopping-problem>.
- 9 See, e.g., Joseph Henchman, *New York Governor Signs Law to Tax Cigarettes Sold on Tribal Lands*, TAX FOUNDATION TAX POLICY BLOG, Dec. 16, 2008, <http://taxfoundation.org/blog/new-york-governor-signs-law-tax-cigarettes-sold-tribal-lands>.
- 10 See Patrick Fleener, *Tax Differentials on the Interstate Smuggling and Cross-Border Sales of Cigarettes in the United States*, TAX FOUNDATION BACKGROUND PAPER No. 16 (Oct. 1, 1996), <http://taxfoundation.org/article/tax-differentials-interstate-smuggling-and-cross-border-sales-cigarettes-united-states>.

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Table 1: 2013 Cigarette Tax Rates, Smuggling Percentages, and Changes Since 2006

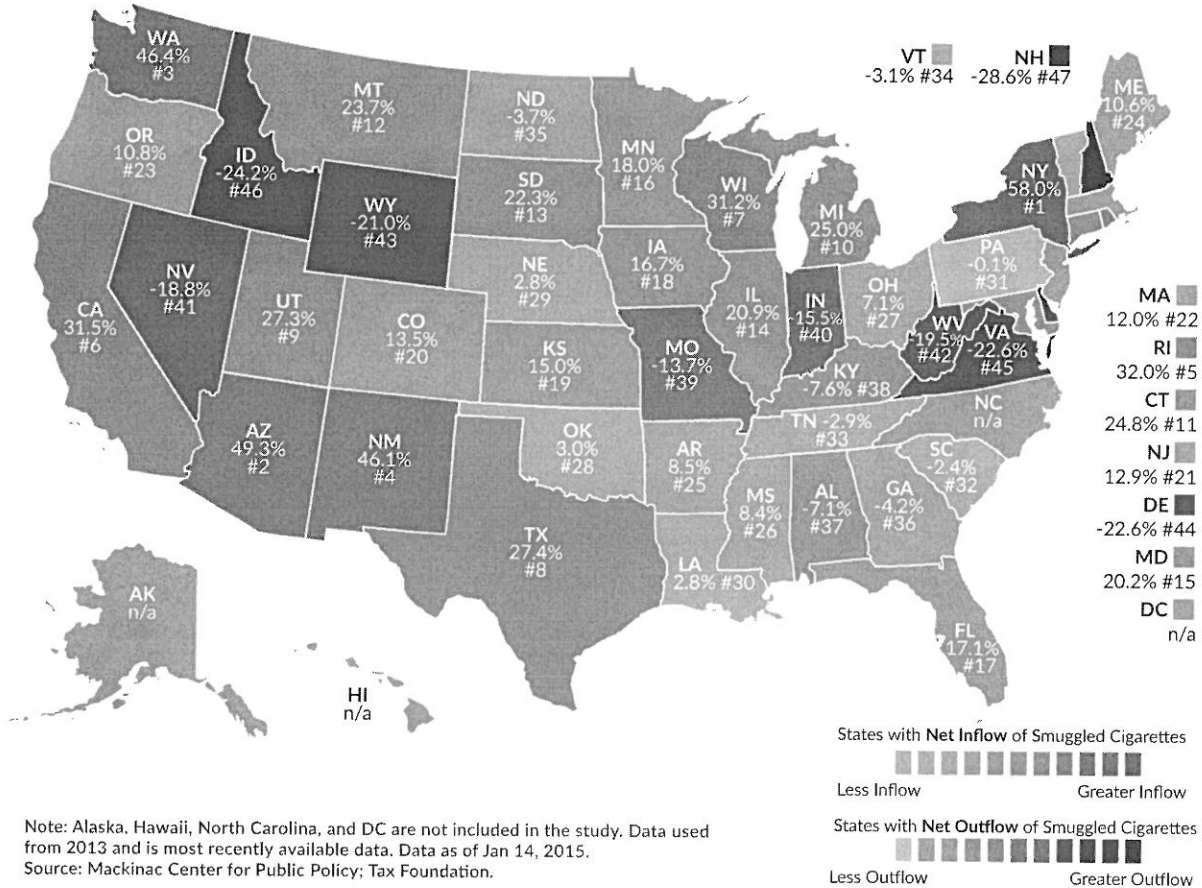
	2013 Tax Rate (per pack)	2013 Consumption Smuggled (positive is inflow, negative is outflow)	2006 Consumption Smuggled (positive is inflow, negative is outflow)	2013 Smuggling Rank (1 is most smuggling, 50 least)	Smuggling Rank Change Since 2006 (e.g., NY rank changed +4)	Cigarette Tax Rate Change, 2006-2013
New York	\$4.35	+58.0%	+35.8%	1	+4	+190%
Arizona	\$2.00	+49.3%	+32.1%	2	+5	+69%
Washington	\$3.025	+46.4%	+38.2%	3	+1	+49%
New Mexico	\$1.66	+46.1%	+39.9%	4	-2	+82%
Rhode Island	\$3.50	+32.0%	+43.2%	5	-4	+42%
California	\$0.87	+31.5%	+34.6%	6	+0	No Change
Wisconsin	\$2.52	+31.2%	+13.1%	7	+11	+227%
Texas	\$1.41	+27.4%	+14.8%	8	+8	+244%
Utah	\$1.70	+27.3%	+12.9%	9	+11	+145%
Michigan	\$2.00	+25.0%	+31.0%	10	-1	No Change
Connecticut	\$3.40	+24.8%	+12.3%	11	+11	+125%
Montana	\$1.70	+23.7%	+31.2%	12	-4	No Change
South Dakota	\$1.53	+22.3%	+5.3%	13	+15	+189%
Illinois	\$1.98	+20.9%	+13.7%	14	+3	+102%
Maryland	\$2.00	+20.2%	+10.4%	15	+9	+100%
Minnesota	\$1.60	+18.0%	+23.6%	16	-6	+1%
Florida	\$1.339	+17.1%	+6.9%	17	+9	+294%
Iowa	\$1.36	+16.7%	+2.4%	18	+15	+278%
Kansas	\$0.79	+15.0%	+18.4%	19	-7	No Change
Colorado	\$0.84	+13.5%	+16.6%	20	-6	No Change
New Jersey	\$2.70	+12.9%	+38.4%	21	-18	+13%
Massachusetts	\$2.51	+12.0%	+17.5%	22	-9	+66%
Oregon	\$1.18	+10.8%	+21.1%	23	-12	No Change
Maine	\$2.00	+10.6%	+16.6%	24	-9	No Change
Arkansas	\$1.15	+8.5%	+3.9%	25	+6	+95%
Mississippi	\$0.68	+8.4%	-1.7%	26	+11	+36%
Ohio	\$1.25	+7.1%	+13.1%	27	-8	No Change
Oklahoma	\$1.03	+3.0%	+9.6%	28	-3	No Change
Nebraska	\$0.64	+2.8%	+12.0%	29	-6	No Change
Louisiana	\$0.36	+2.8%	+6.4%	30	-3	No Change
Pennsylvania	\$1.60	-0.1%	+12.9%	31	-10	+19%
South Carolina	\$0.57	-2.4%	-8.1%	32	+9	+14%
Tennessee	\$0.62	-2.9%	-4.5%	33	+5	+210%
Vermont	\$2.62	-3.1%	+4.5%	34	-4	+46%
North Dakota	\$0.44	-3.7%	+3.0%	35	-3	No Change
Georgia	\$0.37	-4.2%	-0.3%	36	-1	No Change
Alabama	\$0.425	-7.1%	+0.5%	37	-3	No Change
Kentucky	\$0.60	-7.6%	-6.4%	38	+2	+100%
Missouri	\$0.17	-13.7%	-11.3%	39	+5	No Change
Indiana	\$0.995	-15.5%	-10.8%	40	+3	+79%
Nevada	\$0.80	-18.8%	+4.8%	41	-12	No Change
West Virginia	\$0.55	-19.5%	-8.4%	42	+0	No Change
Wyoming	\$0.60	-21.0%	-0.6%	43	-7	No Change
Delaware	\$1.60	-22.6%	-61.5%	44	+3	+191%
Virginia	\$0.30	-22.6%	-23.5%	45	+0	No Change
Idaho	\$0.57	-24.2%	-6.0%	46	-7	No Change
New Hampshire	\$1.68	-28.6%	-29.7%	47	-1	+110%
Alaska	\$2.00	N/A	N/A	N/A	N/A	+25%
Hawaii	\$3.20	N/A	N/A	N/A	N/A	+129%
North Carolina	\$0.45	N/A	N/A	N/A	N/A	+50%
District of Columbia	\$2.50	N/A	N/A	N/A	N/A	+150%

Source: Mackinac Center for Public Policy; Tax Foundation.



## Cigarette Smuggling by State

Smuggled cigarettes consumed as a percentage of total cigarettes consumed, 2013



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