

HB 1175 HD 2

**Measure
Title:**

RELATING TO TAXATION.

**Report
Title:**

Cigarette Tax Increase

Description:

Increases the cigarette tax from 10 cents per cigarette to 20 cents per cigarette beginning July 1, 2009. Effective July 1, 2020. (HB1175 HD3)

LINDA LINGLE
GOVERNOR

JAMES R. AIONA, JR.
LT. GOVERNOR



KURT KAWAFUCHI
DIRECTOR OF TAXATION

SANDRA L. YAHIRO
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**SENATE COMMITTEE ON HEALTH
TESTIMONY REGARDING HB 1175 HD 3
RELATING TO TAX ON TOBACCO PRODUCTS OTHER THAN CIGARETTES**

TESTIFIER: KURT KAWAFUCHI, DIRECTOR OF TAXATION (OR DESIGNEE)

DATE: MARCH 16, 2009

TIME: 2:30PM

ROOM: 016

This measure, proposes to increase the cigarette tax from 10 cents to 20 cents per cigarette starting July 1, 2009. The cigarette tax is currently scheduled to increase to 11 cents per cigarette on September 30.

The Department of Taxation (Department) **opposes this tax increase.**

The Department does not support the tax increase contained in this measure. With the slowing economy impacting struggling families, tax increases should be avoided as much as possible. The Department is also strongly concerned with the timing of this legislation because the state and nation are in a recession where taxpayers are worried about their finances. This tax is highly regressive and will impact the poor the most.

Assuming a current effective date, this measure will result in the following revenue gains:

- \$91.6 million for FY 2010
- \$89.8 million for FY 2011
- \$79.0 million for FY 2012
- \$75.4 million for FY 2013 and after.

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SUBJECT: TOBACCO, Increase tax on cigarettes

BILL NUMBER: HB 1175, HD-3

INTRODUCED BY: House Floor Amendment #3

BRIEF SUMMARY: Amends HRS section 243-3 (a) to increase the tax on cigarettes from 11 cents to 20 cents per cigarette on July 1, 2009.

EFFECTIVE DATE: July 1, 2020

STAFF COMMENTS: The legislature by Act 316, SLH 2006, provided for a staged increase on the tax on cigarettes and provided that any moneys collected in excess of what would have been collected at the tax rate of 7 cents per cigarette are to be distributed to various special funds. While Act 316 also provided staged increases up to 2011 in the distribution of such revenues for the various funds, it provides that between 9/30/08 and 9/29/09: 2.0 cents to be deposited into the Hawaii cancer research fund; 0.5 cents paid into the trauma system special fund; 0.25 cents deposited into the community health centers special fund, and 0.25 cents deposited into the emergency medical services special fund.

If this measure is enacted and takes effect on July 1, 2009, as one section in the bill provides, it would result in an additional 17 cents per cigarette being deposited into the general fund. It should also be remembered that the rising cost of the product may, in fact, jeopardize funding of these programs. In addition, with the federal government's newly adopted increase of \$1.00 per pack, the tax per pack of cigarettes in Hawaii will rise to \$5. As the product becomes more expensive, there will, no doubt, be a reduction in consumption or more untaxed product purchased. This, in turn, will jeopardize the funding of the specified programs making this resource less and less dependable as a funding mechanism for the earmarked programs.

While anti-tobacco advocates might like to see the tax on cigarettes go even high as they believe forcing people to quit smoking is in the best interest of the community, lawmakers must remember that this is a source of revenue that helps to pay the bills. Thus, there is a point of diminishing returns. Consumption has already declined from a high of 54 million packs sold when the tax was a \$1.60 per pack to 50.5 million packs as the tax rose to \$1.80 per pack. It has now leveled off at that level of consumption. Where the revenue line and consumption line will cross is anyone's guess, but at some point, enough people will quit or reduce their consumption of this product where the state will actually realize less revenue even though the tax rate has increased. Caution should be exercised in raising this tax so dramatically at a time when the state general fund is in dire need of resources.

The notion that the state general fund can be balanced with an increase in "sin" taxes on tobacco and alcohol products is ludicrous. First, as noted above, the higher one pushes the cost of these products, the greater the possibility of actually seeing a decline in consumption as consumers moderate or eliminate consumption. Second, much of the consumption of these products, in particular alcoholic beverages, is made by visitors which, as hotels have reported, are dwindling in numbers. Thus, the base for both of these tax resources will begin to shrink until the visitors return. Thus, these tax resources cannot be counted upon to raise revenues to balance the state budget. Thus, legislators will suffer great angst in raising these taxes and will have very little to show for their political risk. In fact, as was evidenced in the

states of New Jersey and Maryland, lawmakers there counted on an increase in the cigarette taxes to help balance their budgets only to learn that collections actually went down below their prior levels. Thus, care should be exercised in targeting these resources for a quick fix to the state's financial woes.

Finally, lawmakers need to remember that the amount payable to the state under the Master Settlement Agreement (MSA) with the tobacco companies is dependent on the amount of product purchased and consumed nationwide. With the rise in the federal tax and potential state tax increases, there is no doubt that it will affect consumption of this product and, therefore, the amount of money the states receive under the MSA.

Digested 3/16/09



Hawai'i Primary Care Association

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To: **The Senate Committee on Health**
The Hon. David Y. Ige, Chair
The Hon. Josh Green, MD, Vice Chair

Testimony in Support of House Bill 1175, HD 2 **Relating to Taxation**

Submitted by Beth Giesting, CEO
March 16, 2009, 3:00 p.m. agenda, Room 016

The Hawaii Primary Care Association urges your support for this measure that would increase taxes on cigarettes. We believe that this is good public health policy and will result in a decrease in smoking. In the meantime, it will also contribute additional general funds for essential State purposes.

Thank you for the opportunity to support this bill.



March 14, 2009

Committee on Health
Senator David Ige, Chair
Senator Josh Green, M.D., Vice Chair

Hearing:

3:00 P.M., Monday, March 16, 2009
Hawaii State Capitol, Room 016

RE: HB1175, HD2, Relating to Taxation

TESTIMONY IN STRONG SUPPORT WITH AMENDMENTS

Once again good afternoon Chair Ige, Vice Chair Green, and members of the Committee on Health. Thank you for the opportunity to testify in strong support of HB1175, HD2, which increases the cigarette tax from 10¢ per cigarette to 20¢ per cigarette beginning July 1, 2009.

Three years ago, the American Cancer Society strongly supported legislation that raised the cigarette tax in Hawaii which allocated a portion of the new revenues raised into the Hawaii Cancer Research Center Special Fund for a new research facility in Kakaako, and operating expenses.

We would like to that this opportunity to briefly note for the committee that numerous economic studies in peer-reviewed journals have documented that cigarette tax or price increases reduce both adult and underage smoking. The general consensus is that every 10% increase in the real price of cigarettes reduces overall cigarette consumption by approximately three to five percent, reduces the number of young-adult smokers by 3.5%, and reduces the number of kids who smoke by 6 or 7%. Also, in filings with the U.S. Securities and Exchange Commission the cigarette companies have publicly admitted the effectiveness of cigarette tax increases to deter smoking.

We believe that this bill will have substantial impact on Hawaii's adult and youth smoking rates. In additional, from what we can determine, it will also generate between \$75 and \$85 million of much needed revenues for our state.

The Society would also request that the committee amend this measure by increasing the tax on other tobacco produces from 40% of the wholesale price to 80% of the wholesale price, with a percentage of the increase going to the Community Health Centers Fund, to ensure the viability of this critical health safety net.

Mahalo for giving me the opportunity to provide testimony in support of this measure here today.

Very truly yours,


A handwritten signature in black ink, appearing to read "G. Massengale".

George S. Massengale, JD
Director of Government Relations



COALITION FOR A
TOBACCO-FREE HAWAII

To: Senator David Y. Ige, Chair, Committee on Ways and Means
Senator Josh Green, M.D., Vice Chair, Committee on Ways and Means
Members, Senate Committee on Health

From: Trisha Y. Nakamura, Policy and Advocacy Director 

Date: March 13, 2009

Hrg: Senate Committee on Health; March 16, 2009; at 3:00 p.m.

Re: **Strong Support for HB 1175 HD 3, Relating to Taxation**

Thank you for the opportunity to testify in strong support of HB 1175, HD 3, which would increase the cigarette tax from 10 cents to 20 cents per cigarette beginning July 1, 2009.

The Coalition for a Tobacco Free Hawaii (Coalition) is the only independent organization in Hawaii whose sole mission is to reduce tobacco use through education, policy and advocacy. Our organization is a small nonprofit organization of over 3,000 partner organizations and advocates that works to create a healthy Hawaii through comprehensive tobacco prevention and control efforts.

Hawaii has the second-lowest number of smoking-related deaths in the nation. Still, tobacco use remains the number one cause of preventable death. Tobacco is responsible for over 1,200 deaths per year in Hawaii and costs over \$330 million dollars in direct medical related costs.

Numerous studies have shown that increasing cigarette taxes is effective at preventing kids from becoming regular, addicted smokers. Price was found to have the greatest impact on preventing youth from becoming daily and relatively heavy daily smokers, with youth being two to three times more sensitive to price changes than adults. Price increases have also been shown to reduce the smoking rates of pregnant women, thus reducing the risk factors for neonatal mortality and other smoking-related complications. We project that with a 20-cents/cigarette tax increase, 8,200 adult smokers will quit and 7,500 residents will be saved from premature smoking-caused death. These declines will ultimately lead to savings from fewer smoking-related and smoking-caused health issues:

- \$2.4 million saved over 5 years from fewer smoking-affected pregnancies and births; and
- \$3.3 million saved over 5 years from fewer smoking-caused heart attacks & strokes.

Some may argue that a tax increase will decrease revenues. However, failure to increase cigarette tax rates results in a revenue loss over time due to inflation and smoking declines. The State ultimately stands to save in smoking-related health costs as smoking rates decline. With a tax of 20-cents/cigarette, we project an additional revenue of \$33.8 million in the first year.

Like the tax increase on smokeless tobacco, increasing the tax on cigarettes is a win-win for our State during this difficult economic time. Please pass this measure out of Committee. Thank you for the opportunity to testify on this matter.



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Testimony In Support of HB 1175, HD 2

The American Heart Association (AHA) of Hawaii strongly supports HB 1175, HD 2. A one time sizeable tax increase would have a greater impact on reducing smoking rates in Hawaii, especially on the lower income and youth markets, which are more price sensitive, and which are the most highly targeted by tobacco company marketing and advertising.

Because smoking levels are highest among people with low incomes, the cigarette companies try to argue that cigarette tax increases are regressive taxes that fall disproportionately hard on lower-income families and communities. But this argument turns reality upside down. These are the same companies that have been preying on low-income and poor communities for decades. In fact, from 1998 to 2002 the cigarette companies increased the prices they charge for their cigarettes by more than \$1.00 per pack (and by more than two cents for every cent needed to cover all of their costs from the state tobacco lawsuit settlements). The cigarette companies have no problem with levying new charges on low-income smokers when it increases their own profits. They only oppose the new charges when someone else (like a state government) gets the new revenues, instead. In fact, even though the federal government's new increase on cigarette taxes has not yet been implemented, the cigarette companies wasted no time after the law passed in hiking the prices on their products to profiteer on the increase.

The fact that smoking rates are highest among lower-income groups means that lower-income families and communities currently suffer the most from smoking and will, consequently, benefit the most from any effective new measures to reduce smoking, including increased state cigarette taxes. Their health problems caused by tobacco use also disproportionately affect Medicaid costs to the state.

Smokers who do not reduce their smoking because of a cigarette tax increase will also still benefit economically, along with every other state taxpayer. Right now, smoking produces a "hidden tax" that totals more than \$40 billion per year to pay for smoking-caused state and federal healthcare costs. Smoking declines caused by state cigarette tax increases directly reduce these smoking-caused tax burdens for all taxpayers.

While tobacco tax increases that raise cigarette prices prevent and reduce smoking among all income groups, they work most powerfully to prompt lower-income smokers to quit or cutback and to stop lower-income kids from every starting. As a result, low-income families and communities will not be the victims of any cigarette tax increase but its biggest beneficiaries.

The cigarette companies' regressivity argument fails to account for each of the following facts:

- Increases to state cigarette tax rates will not place any new financial burdens of any kind on the 85 percent of Hawaii adults who neither smoke cigarettes nor buy them.

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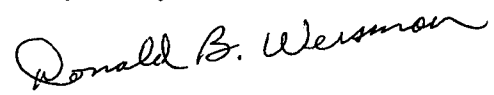
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diseases and stroke."**

- While new cigarette tax increases will raise cigarette prices, many current smokers will avoid the higher prices by quitting, cutting back, or switching to cheaper cigarettes – and lower-income smokers are much more likely than higher-income smokers to quit or cut back in response to price increases. In fact, all of the smokers who quit and many of those who cut back because of cigarette tax increases would actually save money by spending less on cigarettes.
- Those who stopped smoking in response to cigarette tax increases would greatly improve their own health, which could also significantly reduce their healthcare costs. Because of their higher rate of illness and disability, smokers have substantially higher annual and lifetime healthcare costs than nonsmokers or former smokers (despite living shorter lives). Healthcare expenditures caused by smoking total more than \$96 billion per year nationwide, with billions being paid directly by smokers, either through direct healthcare payments or increased health insurance premiums. Tobacco use costs all Hawaii taxpayers and businesses an estimated half-billion dollars each year in smoking-attributable direct medical expenditures and smoking-attributable loss of productivity.
- Any significant state cigarette tax increase also would bring in millions of dollars per year in new government revenues, thereby reducing pressures for other, broader-based tax increases. **Smokers who quit would likely spend the money saved from paying for cigarettes on other products or services that would benefit the state tax coffers without adding to healthcare costs.**
- The smoking declines produced by significant cigarette tax increases save lives, reduce human suffering, promote the public health, and prevent more kids from becoming addicted to smoking or ultimately dying from it – and these results are disproportionately experienced among low-income persons, families, and communities. Even those low-income smokers who do not change their behavior because of tobacco tax increases still benefit from having fewer family members, friends, and neighbors falling victim to tobacco use.
- **The tobacco companies and their front groups will argue that too steep an increase in cigarette prices could negatively impact tax revenue to the state. What they fail to acknowledge is that those who might quit smoking as a result of a tax increase would then have additional money to spend on taxable products that don't result in over a \$500 million in costs to the state. The money doesn't go up in smoke; instead it will likely be spent on more productive things that can benefit our families and our state. Over 5 years, there will be a health savings of \$2.4 million in fewer smoking-affected pregnancies and births, and \$3.3 million from adult and youth smoking declines.**
- **Low-income smokers and their communities disproportionately benefit when the new revenues from cigarette tax increases are directed to programs to help people quit smoking and prevent kids from starting – both because smoking is more prevalent among low-income persons and because they may have much less access or exposure to any such programs than people with higher incomes.**
- Not surprisingly, in poll after poll low-income Americans – along with all other Americans – strongly support higher cigarette taxes in order to prevent and reduce youth smoking.

American Heart Association
March 16, 2009
Page 3

The American Heart Association of Hawaii strongly urges you to support HB 1175, HD 2 and to use the increased tax revenue to increase funding to tobacco prevention and control programs in our state.

Respectfully submitted, -

A handwritten signature in cursive script that reads "Donald B. Weisman". The signature is written in black ink and is positioned above the printed name and title.

Donald B. Weisman
Hawaii Communications and Marketing/Government Affairs Director

From: mailinglist@capitol.hawaii.gov
Sent: Sunday, March 15, 2009 4:37 PM
To: HTHTestimony
Cc: mz9995@hotmail.com
Subject: Testimony for HB1175 on 3/16/2009 3:00:00 PM

Categories: Green Category, Blue Category

Testimony for HTH 3/16/2009 3:00:00 PM HB1175

Conference room: 016
Testifier position: oppose
Testifier will be present: Yes
Submitted by: Michael Zehner
Organization: Individual
Address: 750 Amana st. #608 Honolulu, HI
Phone: 9520275
E-mail: mz9995@hotmail.com
Submitted on: 3/15/2009

Comments:

This is a mean spirited regressive tax on the poor. It proposes changing the State cigarette tax from \$2 to \$4 a pack. It would by far be the meanest in the nation surpassing even New Yorks's tax of \$2.75 per pack.

Let us note that in South Carolina the tax is only 7 cents per pack and in Missouri it is only 17 cents. A tax hike of this magnitude would will have smugglers and the underworld dancing for joy.

This article from the Washington post highlights the danger;

"Cigarette Smuggling Linked to Terrorism

By Sari Horwitz
Washington Post Staff Writer
Tuesday, June 8, 2004; Page A01

Smugglers with ties to terrorist groups are acquiring millions of dollars from illegal cigarette sales and funneling the cash to organizations such as al Qaeda and Hezbollah, federal law enforcement officials say, prompting a nationwide crackdown on black market tobacco.

The federal Bureau of Alcohol, Tobacco, Firearms and Explosives has more than 300 open cases of illicit cigarette trafficking -- including several with terrorist links -- up from only a handful five years ago, ATF sources said.

"This is a major priority for us," said Michael Bouchard, assistant director of the ATF. "The deeper we dig into these cases, the more ties to terrorism we're discovering."

The lucrative trafficking of cigarettes, known as cigarette diversion, is a simple scheme but difficult to stop, law enforcement officials say. The traffickers purchase a large volume of cigarettes in states where the tax is low, such as Virginia and North Carolina, transport them up Interstate 95 to states such as Maryland, New York, Pennsylvania and New Jersey and then sell them at a discount without paying the higher cigarette taxes in those states.

With huge profits -- and low penalties for arrest and conviction -- illicit cigarette trafficking now has begun to rival drug trafficking as a funding choice for terrorist groups, said William Billingslea, an ATF senior intelligence analyst who has studied the issue extensively.

Although black market cigarette sales have been around for decades, the link to suspected terrorist groups is a new and growing phenomenon.

"The schemes provide terrorists millions of dollars which can be used to purchase firearms and explosives to use against the United States and others," said ATF Director Carl J. Truscott, who was appointed to head the agency two months ago after 22 years in the Secret Service.

Several major cases of illicit cigarette trafficking with terrorist links have involved the purchase of cigarettes in Virginia and are currently under investigation, federal law enforcement sources said, adding that there are other cases nationally with links between the traffickers and Hamas, Hezbollah and al Qaeda.

"The money is so lucrative," Billingslea said.

In New York City, for example, where the combined state and city tax on cigarettes is \$3 a pack, a carton can sell for about \$75. The trafficker can buy a carton for about \$20 in Virginia, where the tax is 2.5 cents a pack, and then sell it to a mom-and-pop store in New York at a profit of about \$40 a carton, ATF officials said.

A smuggler can make about \$2 million on a single truckload of cigarettes. A truckload contains 800 cases, or 48,000 cartons.

"People go shopping for a bargain," Billingslea said. "Why pay \$75 for a carton of cigarettes when I know someone down the street who will sell me a carton for \$15 less out of the back of a car?"

The first large-scale cigarette trafficking case tied to terrorism was prosecuted in North Carolina in 2002. A federal jury in Charlotte convicted Mohamad Hammoud, 28, of violating a ban on providing material support to terrorist groups by funneling profits from a multimillion-dollar cigarette-smuggling operation to Hezbollah.

The jury also found Hammoud, whom prosecutors described as the leader of a terrorist cell, and his brother guilty of cigarette smuggling, racketeering and money laundering. The two men, natives of Lebanon, were accused of smuggling at least \$7.9 million worth of cigarettes out of North Carolina and selling them in Michigan. Hammoud was sentenced to 155 years in prison.

Prosecutors were able to prove that profits from the venture were funneled to high-ranking Hezbollah leaders. And Hammoud was caught on wiretaps speaking on the telephone with Hezbollah's military commander in Lebanon, Sheik Abbas Harake, according to trial testimony.

In another case in September, Hassan Moussa Makki, 41, a key player in a multimillion-dollar interstate cigarette smuggling ring, pleaded guilty in Michigan to providing material support for terrorism and participating in a racketeering conspiracy. Prosecutors said he also funneled money to Hezbollah.

Makki, a native of Lebanon, was one of 12 people indicted last year in the scheme to buy low-tax cigarettes in North Carolina and sell them in Michigan. He was sentenced to 57 months in prison.

Law enforcement sources said the terrorist links are established in these and other ongoing investigations through wiretaps and background intelligence investigations and by running the traffickers' names and those of their associates through CIA, FBI and Homeland Security databases. When a terrorist tie is suspected, the cigarette-trafficking probe becomes a joint investigation with one of 66 Joint Terrorism Task Forces across the country. The task forces, run by the FBI, are composed of federal, state and local law enforcement officials.

Paul J. McNulty, the U.S. attorney in Alexandria, last year charged 10 people with possession and distribution of contraband cigarettes, wire fraud and money laundering as part of a scheme to smuggle more than \$2 million in cigarettes bought in Virginia to New York. A man whose name came up in that investigation was arrested in Detroit carrying hundreds of thousands of dollars in wire transfer receipts showing payments to people associated with Hezbollah.

In an interview, McNulty declined to comment on terrorist links in that case. But he said the ATF and other law enforcement agencies are taking cigarette smuggling "more seriously than ever."

"We are pursuing cases such as cigarette smuggling because of the possibility that proceeds from that crime could end up in the hands of terrorists," McNulty said.

He added that the Charlotte case made law enforcement officials more attentive to cigarette smuggling as a key source of financial support for terrorists.

"There are other sources, but this is the one that has gotten the attention of law enforcement," McNulty said.

Cigarette trafficking is difficult to stop, partly because tobacco is a legal commodity. Smuggling cigarettes becomes a federal crime only when more than 60,000 cigarettes, or 300 cartons, are purchased to avoid payment of state tax, said Jerry Bowerman, chief of the ATF alcohol and tobacco enforcement branch.

McNulty said catching the suspects is extremely labor-intensive.

In his case, he said, New York tax authorities placed advertisements in various newspapers and magazines in the New York City area offering Virginia cigarettes for sale. The ads for A&A Tobacco Wholesale listed a Virginia telephone number to place orders. A Virginia post office box was set up as a billing address. Incoming calls were switched to and recorded by an agent with the New York office of tax enforcement.

An undercover storefront location was established for A&A Tobacco Wholesale by law enforcement personnel in King George County in Virginia, where investigators from the New York tax office posed as employees and filled the cigarette orders.

When prospective cigarette purchasers telephoned the advertised number and placed orders, they were told that the cigarettes being sold would bear counterfeit joint New York State and New York City tax stamps.

This is clearly something the anti-smoking lobby is not going to tell you. Do we really want terrorist groups to come to our State to take advantage of something like this.

Respectfully, Michael Zehner