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### News Release

## New York Ignores Its Own History by Implementing Cigarette Tax Hike; Criminal Syndicates Will Benefit More than State Treasury

"One major incentive to organized crime is the high New York City cigarette taxes, piled on top of the state tax, which have made that city the promised land for cigarette bootleggers. ... [A] repeal of these taxes will not promote cigarette smoking. It will merely take cigarette sales from the black market, where they destroy the jobs of honest men and produce crooked profits, and shift these sales to the open market, where they will preserve jobs, promote honest profits, and provide needed public revenues."

-- Gov. Malcolm Wilson, 1974

Washington, D.C., February 29, 2000 -- "Although the nightmarish effects of tax-induced cigarette smuggling have been obvious to the officials and merchants of New York State and City for decades, state officials are ignoring that history by once again raising New York's cigarette excise tax," said Tax Foundation Senior Economist Patrick Fleenor.

The compact, lightweight nature of cigarettes makes them an extremely profitable product for bootleggers. A large tractor trailer truck can hold more than 120,000 packs of cigarettes, and the equivalent of six truckloads of bootleg cigarettes are consumed in New York City every day.

"Profit margins will be in the neighborhood of \$140,000 per truckload when New York's new tax goes into effect," said Fleenor.

Naturally, officials always anticipate higher revenue when they advocate a cigarette tax hike. In New York's case, these projected revenue windfalls have always disappointed. Instead, taxable sales as a percentage of the national average have dropped. This is especially true in New York City, a place where purchases by tourists and commuters should push taxable sales to approximately 120 percent of the national average. Instead they have fallen to less than 70 percent.

In reaction to the disappointing revenue, politicians commonly say that at least the citizens are healthier because they couldn't afford to buy cigarettes. But lower taxable sales don't always mean less smoking, just more cross-border bargain shopping and "discount" cigarettes, i.e. cigarettes from smugglers.

The History of Cigarette Taxes and Smuggling in New York

In a forthcoming history of New York City's cigarette taxation and smuggling, Fleenor traces the association of cigarette taxes with criminal enterprises back to 1939 when New York first passed its cigarette excise tax as a "temporary emergency" funding measure. Soon shoppers were crossing into New Jersey to buy cigarettes, and mail order businesses were advertising their wares in New

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York newspapers. More ominously, organized smugglers began to smuggle large quantities of cigarettes into the state.

These activities were further entrenched when the New York State cigarette tax became permanent in 1947 and then increased by 50 percent a year later. Offers for tax-free cigarettes filled the city's newspapers, and the highway to New York from Virginia, North Carolina, and Washington, D.C. became known as tobacco road as trucks brimming with cigarettes rumbled northward.

New York responded by increasing law enforcement efforts, and over the next 25 years, this became a vicious cycle: higher taxes caused more smuggling, begetting more police action that never succeeded in deterring smuggling. Hijackings became commonplace, and some wholesalers, distributors and trucking firms were forced to move cigarettes in convoys where a delivery truck, which itself had someone "riding shotgun," would be surrounded by more vehicles with armed guards.

A state commission examining cigarette bootlegging cited the case of one trucking company that had to close its doors after 50 years in business after it suffered a rash of hijackings and was unable to obtain insurance. Events such as this prompted City Finance Administrator Roy Goodman to call the illegal cigarette trade the "principal stoking facility of the engine of organized crime."

In March of 1972 the New York State Commission of Investigation released a report stating that the problem of cigarette smuggling in New York state was much more serious than had previously been thought. It estimated that each year from 1966 to 1971, approximately 400 million packs of illegal cigarettes had been smuggled into the state. As a result the State of New York had lost almost \$300 million in revenue, and New York City had lost more than \$90 million.

During the late 1970s and early 1980s, some efforts were made at both the city and state levels to lower or even eliminate the cigarette tax, but they were always defeated. The lesson was partly learned, however, because city officials have not raised their tax since, and state officials held off for almost 20 years. Smuggling continued to worsen, however, and New York City found its taxable cigarette sales falling well below the national average.

On May 1, 1989, New York State raised its cigarette tax again. Accompanying this tax hike was an upsurge in the ancillary crime associated with the illegal cigarette trade. As Robert L. Shepherd, Assistant Deputy Director, Office of Tax Enforcement, New York State Department of Taxation and Finance, pointed out at a meeting of tax administrators that year, high cigarette taxes had created a situation where, "In New York it is literally more profitable to hijack a cigarette delivery truck than an armored truck."

In 1991 the state raised its tax again, and for the next two fiscal years taxable sales in both the state and city continued to plummet. By FY 1997 taxable cigarette sales in both the state and city were at their lowest levels ever compared to the national average: 72.0 percent in the state and 67.1 percent in the city.

The late 1990s have posed their own unique challenges to cigarette tax collection. At internet sites such as [smokemcheap.com](http://smokemcheap.com), the site of the Seneca Indian tribe in upstate New York, cigarettes are

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for sale with no federal, state, or local taxes of any kind, bring the cost of a premium brand down to \$1.70 per pack, or \$1.60 if purchased in bulk (10 cartons or more).

Author of the recent study, "How Excise Tax Differentials Affect Interstate Smuggling and Cross-Border Sales of Cigarettes in the United States," Fleenor points out that the travails of Michigan should be instructive for New York if its own history is an inadequate lesson. Taxable cigarette sales fell 26.7 percent after the state raised its cigarette tax from \$2.50 to \$7.50 per carton. Meanwhile, sales in Indiana and other border states skyrocketed. Similarly, New Hampshire, with its relatively low excise, sells more than twice as many taxable cigarettes as its neighbor Massachusetts despite higher smoking rates in Massachusetts.

The Tax Foundation is a nonpartisan, nonprofit organization that has monitored fiscal policy at the federal, state and local levels since 1937.

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