



## MASSACHUSETTS PACKAGE STORES ASSOCIATION, INC.

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### Retailers Predict Cigarette Tax Increase Would Create Serious Problems for Massachusetts

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Increasing the tax on cigarettes to help subsidize health care has a certain logical appeal, but the policy could have unpleasant side effects.

Experience domestically and in Canada shows that raising cigarette taxes does little to discourage smoking. Higher taxes are, however, a major boon to cross-border and illegal sales, especially sales to minors. Massachusetts lawmakers like to tout the 14% drop in cigarette sales following the state's last 25-cent tax increase in 1993. What they don't mention is that in the same period cigarette sales in New Hampshire rose a whopping 11%.

New Hampshire retailers would surely benefit again if the additional tax were imposed, as the savings would increase to \$6.32-\$10 per carton. Massachusetts smokers who purchase cigarettes tax-free on Indian Reservations in Connecticut, Rhode Island, and New York would save \$8.82 per carton. Per carton savings in other neighboring states would range from \$2.00 in New York and Rhode Island to \$3.46 in Vermont. These savings are just legal incentive for smokers to travel across borders to stock up; illegal sales in-state would surely be ignited, as well.

Price differentials among states invite organized smuggling in cigarettes, just as with other products. With the proposed new tax, Massachusetts would have the second highest cigarette tax in the nation (76 cents per pack, plus sales tax), after Washington State. A 1985 study by the Congressional Advisory Commission found that the "flashpoint" for smuggling is triggered when smokers can save more than \$3.50 per carton by buying on the black market. With a \$6 to \$10 per carton difference between prices in Massachusetts and New Hampshire, smugglers trafficking between the two states would doubtless increase their volume to take advantage of windfall profits. There would also be greater demand for export cigarettes diverted back to the U.S. and for illegal, tax-free imports from overseas; Massachusetts smokers could save more than \$12 per carton buying these products from bootleggers, robbing both the state's treasury and legitimate retailers and wholesalers in the process.

Consider the evidence in Michigan, where cigarette taxes were raised to 75 cents per pack in 1994. Studies show that one in five Michigan smokers participates in the underground cigarette economy, and local officials estimate that about one-third of cigarette sales are now conducted outside legal channels. A flourishing blackmarket also spawns more crime. On top of combating smugglers, Michigan police are facing a rise in retail store break-ins. Frustrated legislators are debating a tax rollback to remedy these dangerous side effects.

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Arizona had similar problems after increasing its cigarette tax by 40 cents per pack. Legal sales tumbled 20-30%, but police had to establish a task force to stem the tide of contraband from California. In Washington State, which has the nation's highest cigarette tax, treasury officials estimate that this year \$65 million (27%) in legal sales will be lost to tax-free Indian Reservations, military bases and cross-border outlets, to say nothing of the loss represented by black market sales conducted in-state. In Washington, as in Michigan and Arizona, legitimate retailers and wholesalers have suffered greatly from cross border sales and the underground market.

In Canada, the government's policy of raising cigarette taxes was an acknowledged disaster, putting an estimated 35% of the country's cigarette sales into the hands of smugglers. In 1994, after the Prime Minister declared that, "Smuggling is threatening the safety of our communities and the livelihood of law-abiding merchants," Canada dramatically reduced its tax and virtually eradicated its black market.

In addition to spawning crime and burdening law enforcement officials, a profitable black market has another detrimental impact: increased sales to minors. Smugglers do not ask for IDs, and teenagers will be among those lining up to buy contraband cigarettes out of the trunks of cars if the new tax is imposed. With organized smugglers at work, it is a myth that higher taxes make cigarettes too costly for kids. In fact, the only way to prevent young people from smoking is through education and by strict enforcement of age laws. One reason Canada's Health Minister Diane Marleau supported her country's decision to slash cigarette taxes was because it would "end the smuggling trade and force children to rely on regular stores." Massachusetts has been making steady progress in reducing sales to minors. Using well-publicized sting operations, local law enforcement officials have brought non-compliance with age restrictions down to 28% statewide. Such efforts would be undermined if more sales were diverted to the blackmarket.

When the negative impact of increased cross-border and blackmarket sales is factored in, the proposed new cigarette tax may not even be the money maker legislators expect it to be. The American Economics Group estimates that legal sales would fall by another 13% if the additional tax were levied. Funding for valuable programs supported by existing cigarette taxes, such as the Health Protection Fund, would decrease by about \$33 million. The drop in sales would also result in \$44 million in lost profits to legitimate retailers and wholesalers, excluding the profits lost on tie-in or sundry product sales at these same outlets. Lost profits of this magnitude would surely result in layoffs of retail and wholesale workers.

How to pay for the health insurance of the growing legion of part time workers is a question of national concern, one which deserves earnest debate and responsible legislative action. However, the state's proposed health care bill and new cigarette tax need reconsideration; as currently written, they would create an entirely new set of serious problems.

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