

**State of Hawaii**  
**Department of the Attorney General**



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**ANNUAL REPORT**  
**OF THE**  
**TOBACCO ENFORCEMENT UNIT**  
**For Fiscal Year 2007-2008**

*Submitted to*  
*The Twenty-Fifth State Legislature*  
*Regular Session of 2009*

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## INTRODUCTION

Section 28-15(d), Hawaii Revised Statutes (HRS), requires the Department of the Attorney General to submit a report to the Legislature, no later than twenty days prior to the convening of each regular session, providing an accounting of the receipts and expenditures of the Tobacco Enforcement Special Fund.

The Tobacco Enforcement Unit (hereinafter referred to as "the Unit") was formed on July 1, 2000,<sup>1</sup> in response to the Attorney General's obligation to enforce the Master Settlement Agreement (MSA); chapter 675, Hawaii Revised Statutes (HRS chapter 675, State's Tobacco Liability Act, "TLA"); and the cigarette tax stamp requirements and prohibition against the sale of prohibited export and foreign cigarettes as codified in chapter 245, Hawaii Revised Statutes (HRS chapter 245).

The Unit consists of a unit supervisor, cigarette tax prosecutor, MSA civil prosecutor, legal clerk, legal assistant, seven criminal investigators, and an auditor.

In fiscal year (FY) 2007-2008, the State received \$56,062,799.06 in MSA settlement moneys. As of the end of June 2008, the State has received a total amount in excess of \$379,000,000 in MSA settlement moneys. In FY 2007-2008, the Unit received \$350,000 in MSA settlement moneys and incurred expenditures of \$289,185 in diligently enforcing HRS chapter 675 and the MSA.

Due to diligent enforcement, cigarette tax revenues for FY 2007-2008<sup>2</sup> totaled \$101,560,051, which represents an increase of \$12,788,385 or approximately 12.6 percent over the comparable period in FY 2006-2007. Moreover, an increase in tax rate coupled with continued vigorous enforcement has significantly contributed to a \$61,500,000 increase in cigarette tax revenues in FY 2007-2008 over the cigarette tax revenues of \$40,049,539 collected in FY 1999-2000. In fiscal year 2007-2008 the Unit incurred expenses of \$678,320 in enforcing HRS chapter 245 and related statutes.

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<sup>1</sup> In keeping with the "diligent enforcement" requirements of the MSA the Department of the Attorney General was engaged in on-going and continuous enforcement efforts prior to the establishment of the Unit in July of 2000.

<sup>2</sup> Section 245-3(a), Hawaii Revised Statutes, sets forth the cigarette tax rates for the relevant period of this report as follows:

- (5) An excise tax equal to 8.00 cents for each cigarette sold, used, or possessed by a wholesaler or dealer on and after September 30, 2006, whether or not sold at wholesale, or if not sold then at the same rate upon the use by the wholesaler or dealer;
- (6) An excise tax equal to 9.00 cents for each cigarette, sold, used, or possessed by a wholesaler or dealer on and after September 30, 2007, whether or not sold at wholesale, or if not sold then at the same rate upon the use by the wholesaler or dealer[.]

**CIGARETTE TAX REVENUES BY FISCAL YEAR:**

FY 1999-2000	\$40,049,539
FY 2000-2001	\$51,739,469
FY 2001-2002	\$62,609,477
FY 2002-2003	\$70,586,392
FY 2003-2004	\$77,541,843
FY 2004-2005	\$83,135,360
FY 2005-2006	\$85,702,483
FY 2006-2007	\$88,771,666
FY 2007-2008	\$101,560,051

**TOBACCO MASTER SETTLEMENT AGREEMENT**

**A. Background**

On November 23, 1998, leading United States tobacco manufacturers, entered into a settlement agreement, entitled the Tobacco Master Settlement Agreement (MSA), with forty-six states, including Hawaii. In consideration for a release of past, present, and certain future claims against them, the MSA obligates these manufacturers to pay substantial sums to the settling states (tied in part to the volume of tobacco product sales). The Attorney General of each state is responsible for enforcing the provisions of the MSA.

**B. MSA Payments<sup>3</sup>**

MSA Payments include three types of payments:

1. **Initial Payments:** The Initial Payments were scheduled to be received annually beginning January 10, 1999 through January 10, 2003. The final Initial Payment was received on January 10, 2003.

FISCAL YEAR	AMOUNT OF INITIAL PAYMENT
1999-2000	\$27,804,177.13
2000-2001	\$11,659,558.77
2001-2002	\$12,701,627.03
2002-2003	\$12,864,378.74
TOTAL	\$65,029,741.67

2. **Annual Payments:** The Annual Payments are received annually beginning April 15, 2000 and on April 15 of each year in perpetuity. The most recent Annual Payment was received on April 17, 2008.

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<sup>3</sup> The reporting of the MSA payments in this year's legislative report differs from years prior to FY 2003-2004 due to adjustments made to the reported figures in order to reflect the receipt of MSA payments strictly on a cash basis as received each fiscal period. In prior reports the MSA payments were reported on a calendar year basis.

FISCAL YEAR	AMOUNT OF ANNUAL PAYMENT
1999-2000	\$20,811,042.90
2000-2001	\$24,471,822.21
2001-2002	\$32,674,220.28
2002-2003	\$31,845,690.90
2003-2004	\$37,793,157.48
2004-2005	\$38,357,998.54
2005-2006	\$35,212,822.31
2006-2007	\$36,857,166.01
2007-2008	\$37,299,996.79
TOTAL	\$295,323,917.42

3. Strategic Contribution Payments: The Strategic Contribution Payments began on April 15, 2008 and are scheduled to be received on April 15 of each year thereafter through 2017. The initial Strategic Contribution Payment was received on April 15, 2008.

FISCAL YEAR	AMOUNT OF STRATEGIC CONTRIBUTION PAYMENT
2007-2008	\$18,762,802.27

TOTAL OF MSA PAYMENTS THROUGH FY 2007-2008

Initial Payments	\$65,029,741.67
Annual Payments	\$295,323,917.42
Strategic Contribution Payments	\$18,762,802.27
TOTAL MSA PAYMENTS	\$379,116,461.36

**C. Duties of the Attorney General and State's Tobacco Liability Act**

In conjunction with the MSA, the Attorney General of Hawaii is tasked with enforcing the State's Tobacco Liability Act (TLA), HRS chapter 675.

The purpose of the TLA is to hold tobacco product manufacturers accountable for the harm caused by the sale of cigarettes to citizens of the State. As stated in section 675-1:

It is the policy of the State that financial burdens imposed on the State by cigarette smoking be borne by tobacco product manufacturers rather than by the State to the extent that such manufacturers either determine to enter into a settlement with the State or are found culpable by the courts . . . . It would be contrary to the policy of the State if tobacco product manufacturers who determine not to enter into such a settlement with the State could use a resulting cost advantage to derive large, short-term profits . . . . It is thus in the interest of the State to require that such manufacturers establish a reserve fund to guarantee a source of compensation and to prevent such manufacturers from deriving large, short-term profits and then becoming judgment-proof before liability may arise.

In FY 2003-2004 the Unit was tasked with the added responsibility of creating and making available for public review a directory of compliant cigarettes and roll your own tobacco products. The directory has been posted on the Internet since October 31, 2003, and has been revised and updated throughout FY 2007-2008. The directory contains information on 35 compliant tobacco product manufacturers and includes a listing of 281 authorized brands of cigarettes and roll your own tobacco products.

### **Enforcement of the MSA and HRS Chapter 675<sup>4</sup>**

A crucial relationship exists between the MSA and the TLA. The MSA and TLA represent affirmative steps toward holding tobacco manufacturers responsible for the many financial burdens imposed on the State. HRS chapter 675 requires any tobacco product manufacturer selling cigarettes to consumers within the State (whether directly or through a distributor, retailer, or similar intermediary or intermediaries) to either become a participating manufacturer and generally perform its financial obligations under the MSA or place funds into an escrow account to establish a reserve fund to guarantee a source of compensation to the State should such tobacco product manufacturers be found culpable by the courts.

With regard to the enforcement of the MSA and HRS chapter 675, in FY 2007-2008 the Unit identified five non-participating manufacturers with sales in the State. A non-participating manufacturer (NPM) is a tobacco product manufacturer who has not entered into the tobacco master settlement agreement, whose product is being sold in the State. In order to identify such NPMs, the Unit has developed a system that:

- (1) Identifies NPMs and their products;
- (2) Gathers and tracks information on NPM products;
- (3) Notifies NPMs of their obligations under HRS chapter 675, HRS chapter 486P, and their related statutes (the Unit accomplished this task by mailing letters to tobacco product manufacturers (worldwide) advising them of the requirements of HRS chapter 675, HRS chapter 486P, and their related statutes);
- (4) Follows through with assistance to effectuate compliance; and
- (5) Provides the information gathering and certification protocols necessary to establish and publish the directory of tobacco product manufacturers whose cigarettes and roll your own tobacco products are authorized to be sold in the State.

How is this accomplished? Armed with a list of wholesalers and distributors the Unit has created a reporting form, mailed the form to the wholesalers and distributors, and started to gather information based on responses and invoices submitted to the Unit by the wholesalers and distributors. Based on the information contained in the invoices the Unit

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<sup>4</sup> It should be noted that during the 2003 regular session two pieces of legislation were introduced and passed (Act 77 and Act 177, Session Laws of Hawaii 2003) that have facilitated the Attorney General's on-going diligent enforcement efforts.

compiled a list of NPMs and their cigarette brands being sold in Hawaii. The Unit's list is supplemented by information from time-to-time from other states that were willing to share their lists of NPMs and brands. In addition, the Unit will continue to actively investigate and identify brands of cigarettes that are on store shelves in an attempt to identify all of the NPMs who have cigarettes for sale in Hawaii.

Ferretting out individual manufacturers and their respective brands is a time consuming process that has been facilitated by the implementation of the directory statute, HRS section 486P-6. Once any tobacco product manufacturer is identified as having sales or intends to have sales within the State, a notice is sent to inform the tobacco product manufacturer that it is required to register with the Unit in compliance with HRS section 486P-5 and comply with all of the requirements of HRS chapter 486P. In the case of NPMs that actually have sales directly or indirectly into the State, sales data is accumulated and formal demands are sent to the NPMs each year requiring that the appropriate sums be placed in a qualified escrow fund in compliance with HRS chapter 675. One obstacle to enforcement efforts is cigarettes ordered and imported into the State by entities other than known wholesalers and distributors. For example, cigarettes are often ordered by consumers or retail stores via the Internet, by phone, or by mail order.<sup>5</sup> Retail inspections are the key to uncovering Internet, phone order, or mail order shipments. In a prior session, the Legislature enacted, Act 131, Session Laws of Hawaii 2005, which went into effect on December 1, 2006, and requires a retail tobacco permit for the sale of any tobacco products. This law requires the retailer to keep records of all tobacco purchases and is designed to address the problem of cigarettes and other tobacco products being acquired from questionable sources resulting in the evasion of the payment of state taxes. There were 1,561 retail permits that were issued statewide as of June 30, 2008. Of that total 63 retail permits were issued for mobile businesses. In past conversations with storeowners, the Unit has learned of another enforcement barrier: peddlers are offering cigarettes bought at military bases to merchants for resale.<sup>6</sup> These two types of cigarette sales are significant because the NPM sales and untaxed cigarette sales affect the amount of moneys available for disbursement under the MSA. An NPM who elects not to join the MSA and who does not comply with the escrow requirements of HRS chapter 675 enjoys a price advantage over compliant tobacco manufacturers. This price advantage has the potential of luring consumers away, thus affecting the market share of the participating manufacturers. The increase of sale of cigarettes by NPMs is not an academic issue. In a recent MSA disbursement, the amounts due to the states were reduced due to a national increase in NPM market share.

It should be noted that the MSA requires the State to "diligently enforce" the requirements of the "model statute" (codified as HRS chapter 675 (TLA)). Failure to "diligently enforce" the TLA may result in a state losing a significant portion of its MSA payments. "Diligent enforcement" in the context of MSA enforcement has not been clearly

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<sup>5</sup> In the 2005 regular session, the Attorney General testified in favor of legislation (see Act 131, Session Laws of Hawaii 2005) that requires a retail tobacco permit for the retail sale of cigarettes and other tobacco products. Act 131 also requires a retailer to keep adequate records to allow law enforcement to determine the source of all cigarettes and other tobacco products sold at retail.

<sup>6</sup> In the 2001 regular session, the Attorney General testified in favor of legislation that further clarified the prohibition against the resale of military cigarettes.

defined. However, we believe that “diligent enforcement” includes:

- (1) Identification of the NPMs and the number of NPM cigarettes sold in the State;
- (2) Notification to the NPMs of their obligations to establish and fund an escrow in accordance with HRS chapter 675; and
- (3) The filing of complaints in court against non-compliant NPMs seeking compliance with the HRS chapter 675.

### **MSA ENFORCEMENT ACTIVITIES IN FY 2007-2008**

- \$56,062,799.06 paid to the State under the MSA.
- Five NPMs sold (whether directly or through a distributor, retailer, or similar intermediary or intermediaries) cigarettes to consumers within the State; all five complied with HRS chapter 675. Status of litigation filed in FY 2006-2007 against five NPMs: one action was settled after full escrow payment and penalty; three actions resulted in default judgments; one action is pending.
- Pursuant to HRS chapter 675, for 2007 sales five NPMs placed \$65,782.67 into qualified escrow funds (100% compliance rate).
- Pursuant to HRS chapter 486P, the Attorney General updated the tobacco directory listing compliant tobacco product manufacturers and their brands.
- Pursuant to HRS chapter 245, only those cigarettes listed in the tobacco directory may be stamped and sold.
- At the end of FY 2007-2008 twenty-seven participating manufacturers were listed in the tobacco directory.
- At the end of FY 2007-2008 eight NPMs were listed in the tobacco directory.

### **CIGARETTE TAX STAMP ENFORCEMENT**

The 2000 Legislature recognized the need for a mandatory cigarette tax stamp system as a means, "to assess, collect, and enforce the cigarette and tobacco tax." The Conference Committee Report on S.B. No. 2486, S.D. 2, H.D. 2, C.D. 1 (2000)<sup>7</sup> noted that the former system of taxation was ineffective and haphazard:

. . . [E]nforcement of the current system of collecting cigarette and tobacco taxes is sporadic, haphazard, and ineffective, resulting in uncollected potential tax revenue. The current system of filing of returns by licensed dealers is in

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<sup>7</sup> Act 249, Session Laws of Hawaii 2000, codified as amendments to HRS chapter 245.

effect a system of voluntary compliance. Persons may try to sell cigarettes and tobacco products without obtaining a license, or could have a license and not file a return or understate the income on the return.

The Legislature also recognized that obtaining actual proof of large-scale black market cigarette sales is nearly impossible due to the nature of the activity, which is necessarily surreptitious, and the limited available resources. Nonetheless, the Legislature concluded that actual proof of magnitude of the black market was unnecessary, "judging from the anecdotal evidence existing and continuing over a fifteen-year period that a black market exists."

With these concerns in mind, HRS chapter 245 was amended to require that the tax imposed under HRS section 245-3, upon the sale or use of cigarettes, shall be paid by licensees through the use of stamps. As a result, beginning January 1, 2001, a licensee or its authorized agent or designee was required to affix a stamp to the bottom of each individual package of cigarettes prior to distribution. Beginning April 1, 2001, no individual package of cigarettes shall be sold or offered for sale to the general public unless affixed with the stamp as required by HRS chapter 245.<sup>8</sup> Diligent enforcement on the part of the Unit has determined the evasion of cigarette taxes as amounting to at least \$22,000,000 annually as reflected by the increase in cigarette tax revenues of \$22,000,000 in FY 2001-2002 over FY 1999-2000.

### **Wholesalers and Distributors**

Beginning in July 2001, the Unit worked closely with the wholesalers and dealers (who were licensed stampers) to facilitate the conversion to stamping. The Unit attended numerous meetings in July and August with the Department of Taxation and the licensed stampers to address questions dealing with tax stamping. The Unit also met with the Department of Taxation and the provider of the tax stamps (Meyercord Corporation) to facilitate the acquisition of a tax stamp for the program. Beginning in January 2001, the Unit began to inspect stampers for compliance with the tax stamp program. Six of the 159 felony arrests for tax stamp violations have involved licensed stampers.

### **Retail Store Inspections and Investigations**

Beginning April 1, 2001, the Unit began a vigorous campaign to seek out those who were violating the cigarette tax stamping requirements of HRS chapter 245.

- There are approximately 1,561 known retail establishments that sell tobacco products: 965 on Oahu, 225 on Hawaii, 189 on Maui, 9 on Lanai, 16 on Molokai, 89 on Kauai, and 68 mobile or lunchwagon type vendors. Inspections have been conducted on the islands of Kauai, Oahu, Maui, Molokai, Lanai and Hawaii. Felony arrests have been made on the islands of Oahu, Maui, Hawaii, Molokai, and Kauai.

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<sup>8</sup> In 2002, the Department of the Attorney General testified in favor of legislation that removed the sunset date of June 30, 2006, from the cigarette tax stamp requirements of HRS chapter 245.

- In FY 2007-2008, 891 retail checks or HRS chapter 245 compliance inspections were conducted statewide.
- There were 41 criminal tobacco investigations in FY 2007-2008 and 619 cartons (the equivalent of 123,800 cigarettes) were seized. Three investigations involved mobile vendors who did not have a retail tobacco permit and two investigations involved the sale of cigarettes or tobacco products by way of ads on Craigslist by individuals who did not have a retail tobacco permit. Thirty-six investigations were the result of cooperative efforts between the U.S. Customs and Border Protection and the Department of the Attorney General and have led to the seizure at the Honolulu International Airport of more than 122,000 contraband cigarettes (611 cartons) from more than thirty individuals.
- Since April 1, 2001, inspections have resulted in over 160 felony arrests and the seizure of over 2,358,873 illegal cigarettes.
- In FY 2007-2008, 5 criminal tobacco prosecutions resulted in \$5,450 in fines. In total, the Unit has prosecuted 122 tobacco cases resulting in criminal fines of \$185,450. In addition, in FY 2007-2008 the Unit's prosecutors successfully prosecuted 15 tax cases, which resulted in criminal fines of \$72,830 and restitution being ordered in the amount of \$263,414 as applicable.
- In total, 54 cigarette prosecutions have resulted in court ordered forfeiture of cigarettes as part of a defendant's criminal sanction. In addition, the Unit's prosecutors have secured 67 civil administrative forfeiture orders or stipulations to the forfeiture of confiscated cigarettes.

### **Coordination with Federal and Other States' Agencies**

The Unit has worked with U.S. Customs and Border Protection in joint investigations of persons smuggling contraband cigarettes into the State from foreign countries. The cooperative effort has resulted in over 30 investigations of individuals who have attempted to bring undeclared or under declared cartons of cigarettes into the State.

It has also interfaced with the Federal Bureau of Alcohol, Tobacco, Firearms, and Explosives of the Department of Justice, the Royal Canadian Mounted Police, and Canadian Customs and Revenue. In addition, the Unit has developed working relationships with the relevant enforcement agencies in the states of California, Oregon, Washington, and Arizona.

### **"Gray Market" or Prohibited Export and Foreign Cigarette Contraband**

"Gray Market" cigarettes clearly marked "Tax Exempt" have been found in the State.<sup>9</sup> These cigarettes are manufactured overseas in such places as: the Philippines, Switzerland,

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<sup>9</sup> In 2001, the Unit confiscated 209 cartons of "Gray Market" cigarettes that were clearly marked "For Export Only" and their sale would have clearly cut into the market share of the participating manufacturers had they made their way into Hawaii's stream of commerce.

China, Southeast Asia, and Colombia representing a multitude of brands and cigarette manufacturers. In order to address the “Gray Market” problem, the Unit has established relationships and is sharing information with the taxing and regulatory authorities in California, Oregon, Washington, Michigan, Florida, Vermont, Utah, Alaska, and Canada. The Unit has also been in contact with the U.S. Postal Service, Federal Bureau of Alcohol, Tobacco, Firearms, and Explosives of the Department of Justice, Internal Revenue Service, U.S. Customs and Border Protection of the Department of Homeland Security, Canadian Customs Service, and the Royal Canadian Mounted Police with regard to “Gray Market” cigarettes and other cigarette-related issues. The Unit is aware of an attempt by certain mainland distributors to mask or re-label “Tax Exempt” cigarettes in order to avoid prosecution for the sale of “Gray Market” cigarettes.

"Gray Market" cigarettes include cigarettes that: have been imported illegally into the United States in violation of federal law; fail to meet federally mandated labeling requirements; or bear an unauthorized brand or trademark. These are the types of cigarettes that are seized in the Unit's joint interdiction efforts with U.S. Customs and Border Protection of the Department of Homeland Security at the airports and are often found at small grocery and liquor stores. These types of cigarettes are most often smuggled into the State from Asia, Southeast Asia, the South Pacific, and the Philippines.

### **Counterfeit Tax Stamps**

Working with the enforcement entities in the states of California, Washington, and Oregon, the Unit has become aware of the presence of counterfeit tax stamps in these jurisdictions. The clear incentive for criminal elements to become involved in counterfeit tax stamping is clear: Hawaii's cigarette tax rate is sixth highest in the nation at \$.10/cigarette or \$2.00/pack of twenty cigarettes.<sup>10</sup> A counterfeit tax stamp that is offered for sale at a price<sup>11</sup> below the \$2.00/pack rate will provide a significant price advantage over vendors who sell properly stamped cigarettes. The Unit continues to be vigilant in searching for any counterfeit Hawaii tax stamps that may be in circulation.

### **Half-Stamping**

Investigations<sup>12</sup> have resulted in arrests for selling half-stamped or partially stamped packs of cigarettes. By placing a half-stamp on the bottom of a package of cigarettes the cigarette tax is being evaded. By placing a half-stamp on the bottom of a pack a vendor is able to stamp two packs for the price of one (i.e., \$1.00 per pack rather than \$2.00 per pack).

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<sup>10</sup> As of August 1, 2008, the Campaign for Tobacco Free Kids reports that the State of New York has the highest tax rate of \$2.75 per pack. New Jersey has the second highest tax rate of \$2.58 per pack. Massachusetts is third with a tax rate of \$2.51 per pack. Fourth is Rhode Island with a tax rate of \$2.46 per pack. Washington State's tax rate is fifth at \$2.25. Alaska, Arizona, Connecticut, Maine, Maryland, and Michigan are tied at sixth with tax rates of \$2.00 per pack. Hawaii will also be ranked sixth effective September 30, 2008, with an effective tax rate of \$.10 per stick or \$2.00 per pack.

<sup>11</sup> Counterfeit tax stamps may range in price from \$.03 to \$.50 per stamp.

<sup>12</sup> Arrests were made for half-stamping in November 2001. At that time, the Unit seized 12,879 packs, of which 2,639 packs were half-stamped and 10,240 packs were unstamped.

## Continuing Enforcement

In order to continue its enforcement activities the Unit will be conducting surprise inspections of: wholesalers and distributors; cigarette vending machines; and retail establishments throughout the State for HRS chapter 245 compliance. Efforts continue both in Hawaii and on the national stage to address the problems posed by the Internet sale of cigarettes. Hawaii continues to cooperate with other states in facilitating the agreements reached between the states and the major credit card companies that prohibit the use of credit cards in the purchase of cigarettes by way of the Internet and through the mail.

## Cigarette Tax Revenues

There has been a significant increase in the cigarette tax revenues since the implementation of the Tax Stamp program on January 1, 2001. For the fiscal year that ended June 30, 2001, cigarette tax revenues were \$11,689,930 or 29 percent higher than they were in FY 1999-2000 even though the tax stamp program was in effect only half of the fiscal year and effective enforcement began at the retail level with only three months left in the fiscal year:

FY 1999-2000	FY 2000-2001	INCREASE
\$40,049,539	\$51,739,469	\$11,689,930

The increase is even more dramatic when comparing the fiscal period ending June 30, 2002, to those collected in 2000. The State collected \$62,609,477 in cigarette tax revenues for FY 2001-2002. The State collected \$40,049,539 in cigarette tax revenues over the same period in FY 1999-2000. Diligent enforcement yielded an increase of over \$22,000,000 or approximately 56 percent:

FY 1999-2000	FY 2001-2002	INCREASE
\$40,049,539	\$62,609,477	\$22,559,938

The \$22,559,938 in increased cigarette tax revenues provides clear evidence that the sale of untaxed cigarettes was firmly entrenched and flourishing with sales of at least 22,559,938 packs or 2,255,993 cartons of cigarettes. The quantity of previously untaxed cigarettes would easily fill 46 forty-foot shipping containers.<sup>13</sup>

Due to diligent enforcement, cigarette tax revenues for FY 2007-2008<sup>14</sup> totaled \$101,560,051, which represents an increase in revenue of \$12,788,835 or approximately 12.6 percent over the comparable period in FY 2006-2007.<sup>15</sup> Moreover, an increase in tax rate

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<sup>13</sup> Each forty-foot container holds 960 master cases containing 50 cartons each.

<sup>14</sup> The cigarette tax rate of \$.07 per stick (\$1.40 per pack), which became effective on July 1, 2004, increased to \$.08 per stick (\$1.60 per pack) on September 30, 2006, \$.09 per stick (\$1.80 per pack) on September 30, 2007, and \$.10 (\$2.00 per pack) on September 30, 2008.

<sup>15</sup> Cigarette tax revenue for FY 2006-2007 stood at \$88,771,666.

coupled with continued vigorous enforcement has significantly contributed to a \$61,500,000 increase in cigarette tax revenues in FY 2007-2008 over the cigarette tax revenues of \$40,049,539 collected in FY 1999-2000.

FY 1999-2000	FY 2007-2008	INCREASE
\$40,049,539	\$101,560,051	\$61,510,512

**FUNDING FOR FY 2007-2008:**

MSA enforcement funds: \$350,000

Cigarette tax stamp fees/interest/fines: \$1,502,746

Total funding: \$1,852,746

**APPROPRIATIONS AND EXPENDITURES FOR FY 2007-2008:**

Appropriations for FY 2007-2008: \$1,257,964

- The Legislature appropriated \$1,257,964 for MSA and cigarette tax stamp enforcement for FY 2007-2008.
- The appropriation to be funded with \$350,000 from moneys received from the MSA and \$907,964 from cigarette tax stamp fees.

Expenditures for FY 2007-2008: \$1,075,675

- MSA Enforcement: \$342,951
- Cigarette Tax Stamp Enforcement: \$732,724

**TOBACCO ENFORCEMENT UNIT'S EXPENDITURES FY 2007-2008**

	<u>MSA</u>	<u>TAX STAMP</u>
<b>APPROPRIATION</b>	\$350,000.00	\$907,964.00
<b>PERSONNEL COSTS</b>		
SALARIES AND FRINGE	\$219,677.83	\$597,640.69
<b>OPERATIONAL EXPENSES &amp; OVERHEAD COSTS</b>		
LEASE RENT	\$42,024.12	\$42,024.12
FURNITURE, FIXTURES, & EQUIPMENT	-----	-----
COMPUTERS	-----	-----
TRAVEL	\$7,587.32	\$10,400.68
PHONES	\$1,396.88	\$7,378.00
OFFICE EQUIPMENT	\$2,512.62	\$2,511.68
SUPPLIES	\$1,303.95	\$1,606.13
INVESTIGATION EQUIPMENT	-----	-----
TRAINING/CONFERENCE	-----	-----
EVIDENCE STORAGE	-----	-----
MILEAGE	-----	\$9,892.92
MISC. EXPENSES	\$1,127.28	\$2,073.09
LITIGATION EXPENSES	\$8,124.90	
ADMINISTRATION EXPENSES (EST. ALLOCATION)	<u>\$59,196.50</u>	<u>\$59,196.50</u>
<b>TOTAL OPERATIONAL EXPENSES &amp; OVERHEAD COSTS</b>	\$123,273.57	\$135,083.12
<b>TOTAL EXPENSES</b>	<u>\$342,951.40</u>	<u>\$732,723.81</u>
<b>APPROPRIATION BALANCE<sup>16</sup></b>	<u>\$7,048.60</u>	<u>\$175,240.19</u>

**CONCLUSION**

The unit's activities are critical and time-sensitive if the State is to receive its fair share of the "Tobacco Settlement Funds" as a result of diligent enforcement of the MSA, HRS chapter 675, and related statutes.

Effective enforcement of the State's Gray Market Statute, Cigarette Tax Stamp requirements, Tobacco Permit requirements, and a comprehensive regulatory environment will allow the Unit to identify and address any problems that the State may have with contraband cigarette sales and increase State tax revenues by providing a more effective means to assess, collect, and enforce the provisions of HRS chapter 245 and related statutes.

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<sup>16</sup> Imbedded in the appropriation balances of \$182,289 are personnel costs that were not incurred due to positions not being filled for the entire fiscal year (2 Investigator V positions and 1 Auditor position are to be filled). As a result, funds that would otherwise have been used for these positions' salaries and fringe benefits reverted to the Tobacco Enforcement Special Fund.