



## **SJR 21: Illegal Cigarette Trafficking**

November 13, 2012

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# Overview



- Study Authorization
- Summary
- Virginia Dept. of Taxation Data
- Enforcement and Conviction Data
- Policy Considerations
- Discussion

# Study Authorization



- Senate Joint Resolution 21 (Illegal Cigarette Trafficking) was introduced by Senator Howell during the Regular Session of the 2012 General Assembly.
- The resolution specifically directs focus upon a number of issues related to cigarette trafficking, including methods used, why it occurs, who is engaging in this area of crime, and statutory options to combat the problem.

# Summary



- Tobacco tax revenue is an integral part of Virginia's economy.

	Cigarette Tax	OTP Tax	MSA Payments
<b>Fiscal Year 2010</b>	\$ 158.4 million	\$17.7 million	\$121.6 million
<b>Fiscal Year 2011</b>	\$ 155.7 million	\$18.0 million	\$115.1 million
<b>Fiscal Year 2012</b>	\$ 174.0 million	\$18.7 million	\$117.4 million

Source: Virginia Department of Taxation

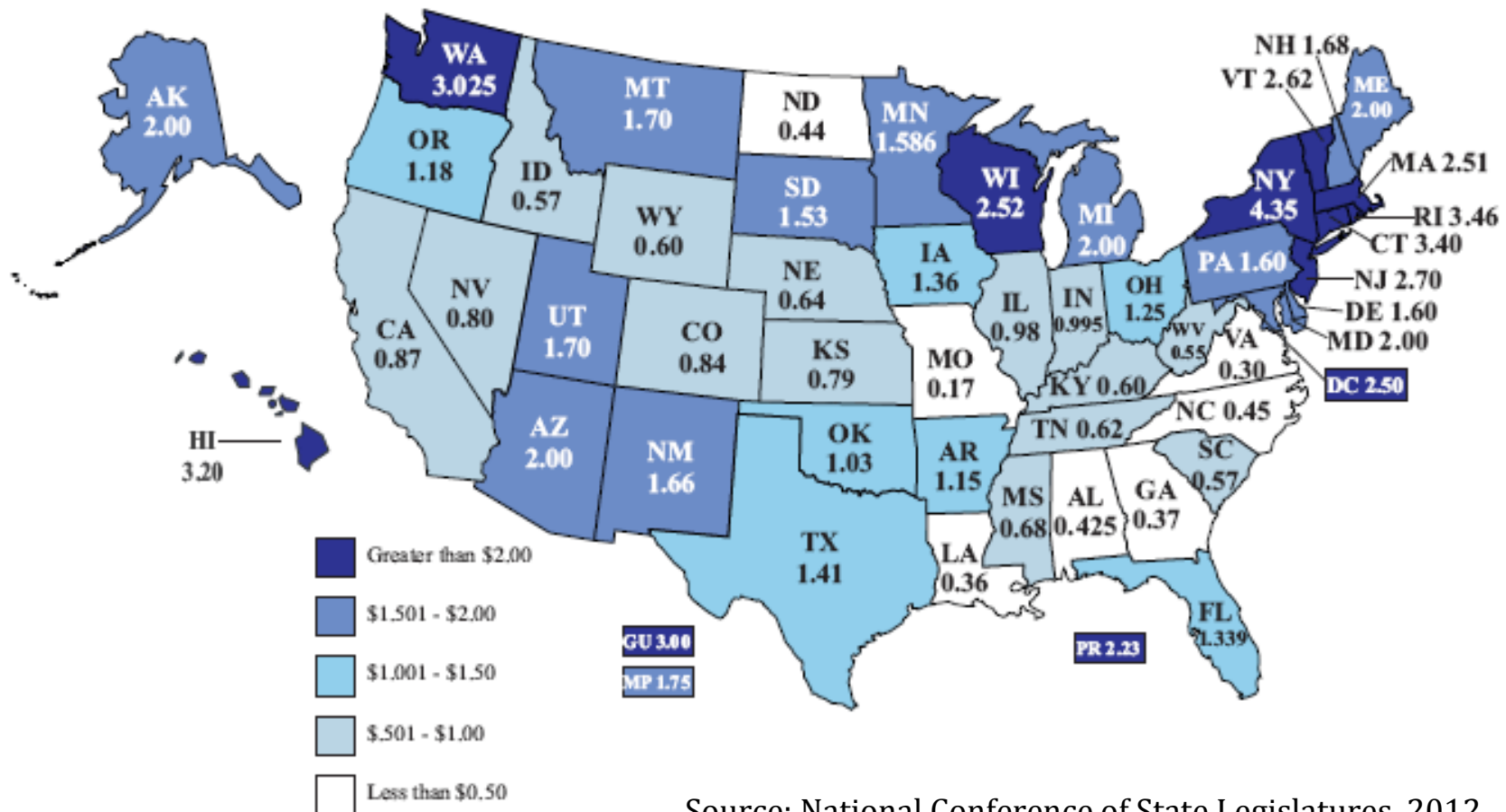
# Summary



- All cigarette trafficking schemes, no matter the methods employed, depend upon tax avoidance.
- Cigarette smuggling and “black market” cigarettes have existed for decades, but recent tax increases in a number of states have greatly increased the potential profits to be made.

# Summary

## Enacted State Cigarette Excise Tax Rates - 2011



Source: National Conference of State Legislatures, 2012

# Summary



- The state excise tax rate for a carton of cigarettes (10 packs):
  - **Virginia:**               **\$3.00**
  - Pennsylvania:       \$16.00
  - New Jersey:       \$27.00
  - Rhode Island:     \$34.60
  - New York:         \$43.50
  - **New York City:   \$58.50**

# Summary



State	State Excise Tax Rate/carton		<u>Per Carton</u> Differential		<u>Per Case</u> Differential
Virginia	\$3.00	→	N/A	→	N/A
Pennsylvania	\$16.00	→	\$13.00	→	\$780.00
New Jersey	\$27.00	→	\$25.00	→	\$1,440.00
Rhode Island	\$34.60	→	\$31.60	→	\$1,896.00
New York	\$43.50	→	\$41.50	→	\$2,430.00
New York City	\$58.50	→	\$55.50	→	\$3,330.00

Source: National Conference of State Legislatures, 2012



# Summary



- The profit on a diverted load of 1,500 contraband cartons of cigarettes, taken from Virginia to New York City, can approach \$100,000, due to differences in tax rates.
- The profit margin for trafficked cigarettes is now higher than for cocaine, heroin, marijuana, or firearms.
- Studies estimate that between 9% and 20% of all cigarettes in New York City originated from Virginia.

# Summary



Source: Seized by Maryland and NVCTB

# Summary



- Trafficking hurts all legitimate manufacturers, wholesalers, and retailers, who are faced with unfair competition in the form of lower prices offered by their competitors.
- Staff has received anecdotal information that in certain areas of Virginia, large numbers of individual retailers have been forced out of business by competitors who profit from trafficking.

# Summary



- Law enforcement, both in Virginia and nationally, have noted that organized crime has moved into the business of cigarette trafficking.
- There are reports that criminals formerly involved with drug smuggling have switched to cigarettes.
  - Just as much money, less violence, and much less prison time if caught.
- As organized crime turns to Virginia for its supplies of cigarettes, there is an increase in attendant crimes:
  - Identity theft/credit card fraud; money laundering; burglaries and robberies of other criminals.

# Summary



- While no precise figures can be ascertained, it seems clear, from law enforcement reports and rudimentary data calculations, that illegal cigarette traffickers are generating at least tens of millions of dollars a year in Virginia.

# Summary



- Conclusion: Illegal cigarette trafficking is not a “cigarette issue.”
- IT IS AN ORGANIZED CRIME ISSUE.

# Summary



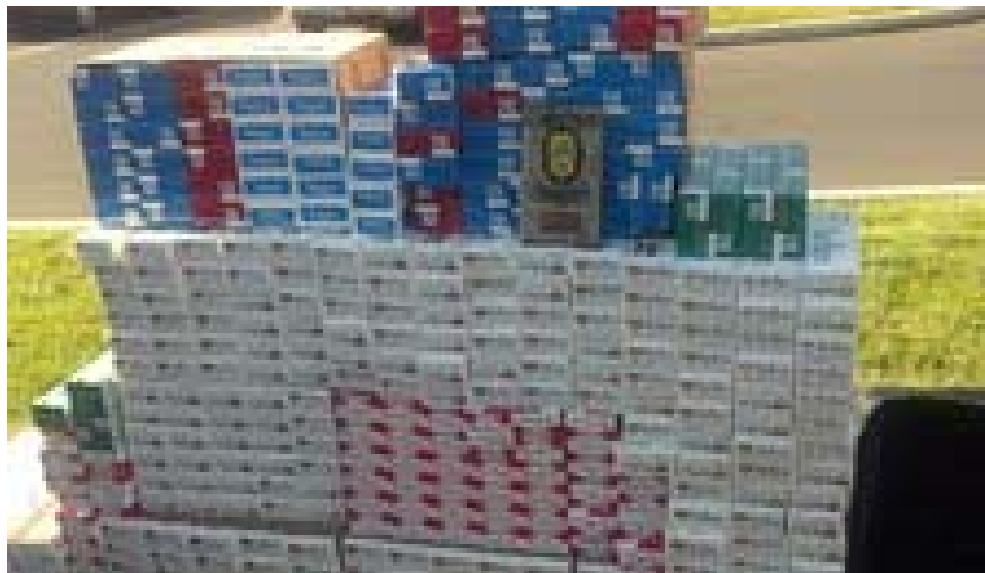
- “ATF agents stopped a Lincoln Town car in Richmond, loaded down with 1,800 cartons of smuggled cigarettes.”
  - ABC7, Kris Van Cleave, November 9, 2012.
- “Maryland’s comptroller said about 8,000 packs of contraband cigarettes worth about \$52,000 were seized from a car on Interstate 70 in Hagerstown. Comptroller Peter Franchot said agents pulled over a vehicle registered in New Jersey on Thursday and confiscated the illegal cigarettes.”
  - WBALTV, November 9, 2012.



# Summary



- Large quantities of cigarettes continue to be seized en route from Virginia to New York and New Jersey.



Source: Northern Virginia Cigarette Tax Board, November 9, 2012.



# Virginia Dept. of Taxation Data



## Total Number of Tax Stamps Sold, FY02-FY12

Fiscal Year	# Stamps Sold
2002	662,103,280
2003	686,260,000
2004	719,601,000
2005	616,991,000
2006	597,167,000
2007	581,314,000
2008	567,491,000
2009	570,374,040
2010	543,309,500
2011	536,652,320
2012	585,868,400

Source: Virginia Department of Taxation

# Virginia Dept. of Taxation Data



## Total Cigarette Tax Stamp Revenue Collected, FY02-FY12

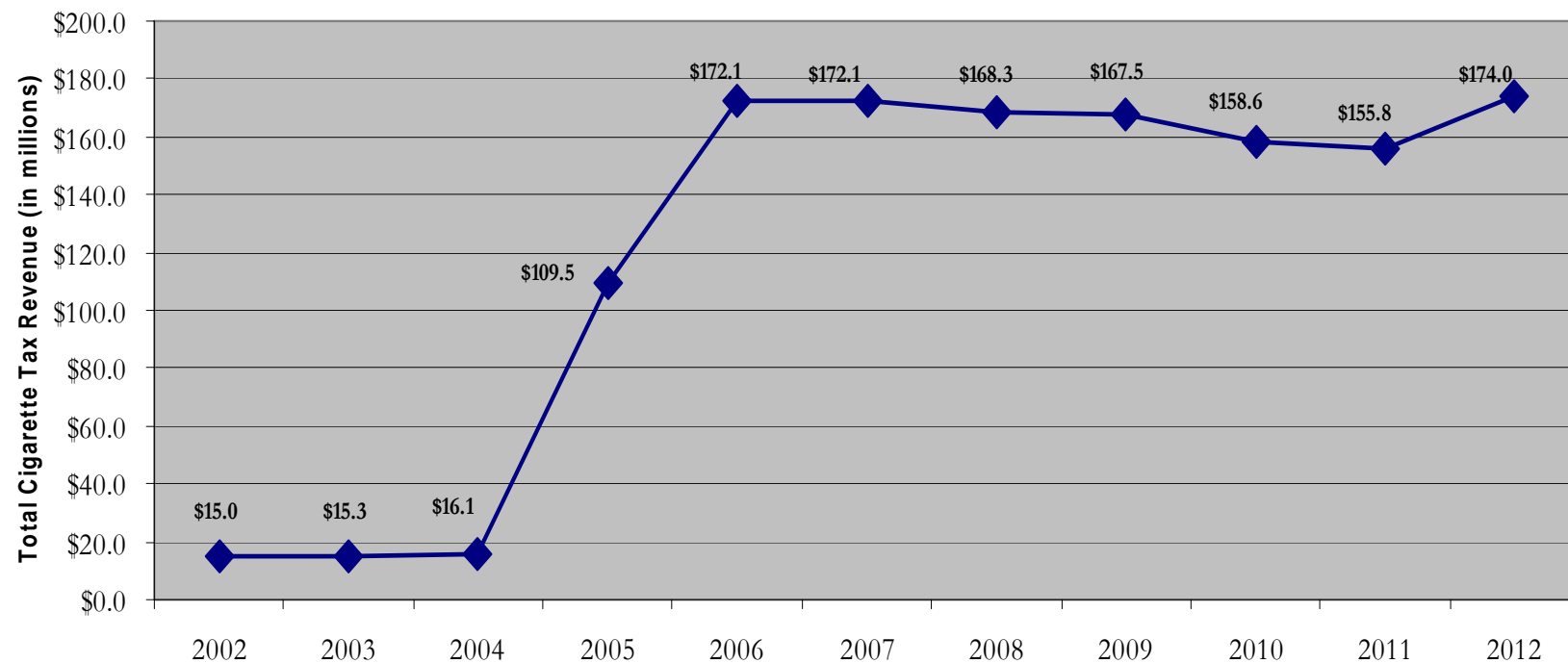
Fiscal Year	Cigarette Tax Revenue (Gross \$)
2002	\$ 15.0 million
2003	\$ 15.3 million
2004	\$ 16.1 million
2005	\$ 109.5 million*
2006	\$172.1 million**
2007	\$ 172.1 million
2008	\$ 168.3 million
2009	\$ 167.5 million
2010	\$ 158.6 million
2011	\$ 155.8 million
2012	\$ 174.0 million

Source: Virginia Department of Taxation. \* Rate increased from \$0.025 to \$0.20 effective 9/1/04; \*\* Rate increased from \$0.20 to \$0.30 per 20 cigarettes effective 7/1/05.

# Virginia Dept. of Taxation Data



Total Cigarette Tax Stamp Revenue Collected, FY02-FY12



Source: Virginia Department of Taxation, Table reflects gross revenues collected.

# Virginia Dept. of Taxation Data



- Estimated Sales Tax revenue collected from cigarettes.

	FY2011	FY2012
<b>General Fund (3.5%)</b>	\$85.13 million	\$95.96 million
<b>Transportation Trust Fund (0.5%)</b>	\$ 12.23 million	\$13.79 million
<b>Local Sales Tax (1%)</b>	\$24.46 million	\$ 27.57 million
<b>TOTAL SALES TAX REVENUE</b>	<b>\$121.82 million</b>	<b>\$137.32 million</b>

Source: Virginia Department of Taxation

# Enforcement and Conviction Data



- The Virginia Department of Taxation audits cigarette wholesalers, and conducts site inspections at retailers who are known to sell cigarettes.
  - No wholesaler licenses have been revoked in the past two years.
  - There have been over 1,400 retail site inspections since 2010.

# Enforcement and Conviction Data



- Approximately 100 warning letters have been issued to retailers by the Virginia Department of Taxation in the past three years.
- In the past two years, the Department has issued 201 assessments for cigarette related violations, and collected \$112,500 in penalties from retailers.

# Enforcement and Conviction Data



- The Northern Virginia Cigarette Tax Board makes approximately 3,000 inspections of retail establishments per year across 17 jurisdictions.

Calendar Year	Total Packs Seized*
2007	9,320
2008	7,936
2009	18,159
2010	25,568
2011	22,777
2012	12,989**

Source: Northern Virginia Cigarette Tax Board. \*Numbers are approximate

\*\*As of September 2012.

# Enforcement and Conviction Data



- The Northern Virginia Cigarette Tax Board works closely with the Comptroller of Maryland to interdict trafficked cigarettes.
- <http://www.wjla.com/articles/2012/11/only-on-7-undercover-maryland-investigators-close-in-on-a-suspected-smuggler--81899.html>



# Enforcement and Conviction Data



## Comptroller of Maryland- Field Enforcement Division Data for Possession & Transportation of Va. Stamps into Maryland

Fiscal Year	Arrests	Packs	Value	Tax Loss	Convicted	Not Convicted
2008	13	43,612	\$ 214,722.24	\$ 83,014.00	6	7
2009	39	161,420	\$ 821,442.57	\$317,319.00	22	15
2010	23	64,605	\$ 485,995.95	\$ 145,680.97	9	11
2011	47	177,332	\$ 1,028,097.76	\$ 354,845.82	32	15
2012	109	315,936	\$ 1,899,541.64	\$631,832.00	53	56
<b>Totals</b>	<b>231</b>	<b>762,905</b>	<b>\$4,449,800.16</b>	<b>\$ 1,532,691.79</b>	<b>122*</b>	<b>104*</b>

Source: Comptroller of Maryland- Field Enforcement Division. \* The figures only identify individuals charged with the felony charge of "transporting contraband cigarettes in the State of Maryland," and not those charged with misdemeanor possession.

# Enforcement and Conviction Data



- Virginia State Police's Criminal Interdiction and Counter-terrorism Unit (CCI) reported that from January 2012- October 2012 approximately 1,941 cartons and \$226,360 were seized as a result of their normal drug interdiction efforts.
  - However, these figures do not represent total VSP Department action regarding cigarette smuggling.

# Enforcement and Conviction Data



- Virginia has taken a meaningful step towards combating cigarette trafficking, with the enactment of Va. Code § 58.1-1017.1, which went into effect on July 1, 2012.
  - Criminalizes the possession of 25 or more stamped cartons of cigarettes, by non-authorized holders, with the intent to distribute.

# Enforcement and Conviction Data



- Because it has been in effect for a little over four months, there is no meaningful data available on its use by law enforcement or prosecutors.
  - Newspaper accounts indicate there have been some arrests under the statute.

# Enforcement and Conviction Data



- Available general district court data indicate that no charges have been filed for the following statutes since FY2008:
  - § 3.2-4209.1- False information on any return by Tobacco manuf/importer.
  - § 3.2-4219- False statement in record required by TSA.
  - § 4.1-103.01(C)- Divulge information provided by tax commissioner.
  - § 18.2-246.13 (E, F, G, H)- Fail to register before delivery of cigarettes; False statement filed, required before delivery of cigarettes; Fail to report cigarette delivery; False statement on report required after delivery of cigarettes.
  - § 58.1-1006- Interfering with enforcement of cigarette excise tax.
  - § 58.1-1008.1- Manufacturer fails or refuses to file report with Tax Dept.; Manufacturer refuses audit or inspection of records by Tax Dept.
  - § 58.1-1008.2- False statement in record required for cigarette tax.
  - § 58.1-1009- Cigarettes, unlawful sale of revenue stamps.
  - § 58.1-1010- Illegal sale of unstamped cigarettes by wholesale dealers.
  - § 58.1-1011- False/fraudulent statement in application for stamping permit.
  - § 58.1-1021- Fail to keep records on purchase, sale of cigarettes (Use Tax).
  - § 58.1-1021.04:1- False/fraudulent statement in application for distributor's license.
  - § 58.1-1034- Violation of reporting requirements.

# Enforcement and Conviction Data



## General District Court- Total Charges and Convictions, FY08-FY11

Statute	FY2008	FY2009	FY2010	FY2011
§ 3.1-336.10(D,i)/ § 3.2-4212(D,i)- Sell or distribute cigarettes not in directory	0	20 charges 1 conviction	N/A	N/A
§ 3.2-4212(D,ii)- Possess, import, etc., cigarettes not in directory, <3000 pkgs.	N/A	N/A	0	1 charge 2 convictions*
§ 4.1-103.01(B)- Dealers fail to allow inspection of records	0	0	0	1 charge 0 conviction
§ 58.1-1007- Fail to keep records on purchase, sale of cigarettes (Excise Tax)	0	0	0	1 charge 1 conviction

Source: Virginia Criminal Sentencing Commission.

\* Fiscal year in which the charge was concluded, which may differ from year charge was initiated.

\*\* Data do not include charges that were still pending at the end of FY11. Includes charges and convictions for subsequent offenses.

# Enforcement and Conviction Data



## General District Court- Total Charges and Convictions, FY08-FY11

Statute	FY2008	FY2009	FY2010	FY2011
§ 58.1-1017(B)-Cigarettes without stamp, sale, purchase, possess, < 3,000 pkgs.	7 charges 4 convictions	32 charges 5 convictions	21 charges 10 convictions	7 charges 7 convictions
§ 58.1-1017(C)-Cigarettes without stamp, sale, purchase, possess, > 3,000 pkgs.	0	3 charges 0 convictions	2 charges 0 convictions	10 charges 0 convictions
§ 58.1-1033-Violation of restrictions	0	1 charge 0 convictions	0	3 charges 0 convictions
Local Cigarette Tax Ordinance Violation	4 charges 3 convictions	105 charges 28 convictions	158 charges 33 convictions	107 charges 36 convictions

Source: Virginia Criminal Sentencing Commission.

\* Fiscal year in which the charge was concluded, which may differ from year charge was initiated.

\*\* Data do not include charges that were still pending at the end of FY11. Includes charges and convictions for subsequent offenses.

# Enforcement and Conviction Data



Available circuit court data indicate that no charges have been filed for the following statutes since FY2008.

- § 3.2-4212(D,i)/ § 3.1-336.10(D,i)- Sell or distribute cigarettes not in directory, <3,000 and < 3,000 pkgs.
- § 3.2-4212(D,ii)/ § 3.1-336.10(D,ii)- Possess, import, etc., cigarettes not in directory, <3,000 and < 3,000 pkgs.
- § 3.2-4209.1- False information on any return by Tobacco manuf/importer.
- § 3.2-4219- False statement in record required by TSA.
- § 4.1-103.01(B)- Dealers fail to allow inspection of records.
- § 4.1-103.01(C)- Divulge information provided by tax commissioner.
- § 18.2-246.13 (E, F, G, H)- Fail to register before delivery of cigarettes; False statement filed, required before delivery of cigarettes; Fail to report cigarette delivery; False statement on report required after delivery of cigarettes.
- § 58.1-1006- Interfering with enforcement of cigarette excise tax.
- § 58.1-1007- Fail to keep records on purchase, sale of cigarettes (Excise Tax).
- § 58.1-1008.1- Manufacturer fails or refuses to file report with Tax Dept.; Manufacturer refuses audit or inspection of records by Tax Dept.
- § 58.1-1008.2- False statement in record required for cigarette tax.
- § 58.1-1010- Illegal sale of unstamped cigarettes by wholesale dealers.
- § 58.1-1011- False/fraudulent statement in application for stamping permit.
- § 58.1-1021- Fail to keep records on purchase, sale of cigarettes (Use Tax).
- § 58.1-1021.04:1- False/fraudulent statement in application for distributor's license.
- § 58.1-1034- Violation of reporting requirements.



# Enforcement and Conviction Data



## Circuit Court- Total Charges and Convictions, FY08-FY12

Statute	2008	2009	2010	2011	2012
§ 58.1-1009-Cigarettes, unlawful sale of revenue stamps	0	0	0	1 charge 1 conviction	0
§ 58.1-1009-Revenue stamps not purchased from Tax Dept.	0	0	0	8 charges 4 convictions	0
§ 58.1-1017(B)-Cigarettes without stamp, sale, purchase, possess, < 3,000 pkgs.	1 charge† 0 convictions	0	8 charges† 7 convictions†	11 charges 6 convictions	4 convictions*
§ 58.1-1017(C)-Cigarettes without stamp, sale, purchase, possess, > 3,000 pkgs.	0	0	0	32 charges 8 convictions	12 charges 1 conviction
§ 58.1-1033-Violation of restrictions	0	0	0	1 charge 0 convictions	0
Local Cigarette Tax Ordinance Violation	3 charges† 3 convictions†	0	0	0	0

Source: Virginia Criminal Sentencing Commission.

\* Fiscal year in which the charge was concluded, which may differ from year charge was initiated.

\*\* Data do not include charges that were still pending at the end of FY12. Includes charges and convictions for subsequent offenses. † These charges were the result of appeals from General District Court.

# Policy Considerations



**ISSUE 1:** Increase the penalties for possession of stamped cigarettes with the intent to unlawfully distribute.

- Option 1: Raise the current penalty of Va. Code § 58.1-1017.1, from a Class 2 misdemeanor to a Class 1 misdemeanor.
  - The penalty for a second offense could then be increased to a Class 6 felony.
- Option 2: For large quantities of cigarettes, make a first offense a Class 6 felony.
  - Possibilities: 50 cartons (federal jurisdiction limit), 60 cartons, 75 or more cartons.
  - The penalty for a second offense could then be increased to a Class 5 felony.

# Policy Considerations



**ISSUE 2:** Increase the penalties for possession of unstamped cigarettes with the intent to evade payment of taxes.

- Option 1: Lower the felony threshold level under Va. Code § 58.1-1017, from 3000 packs (300 cartons) to 500 packs (50 cartons), which is the quantity that is a felony under federal law.
- Option 2: Make a second or subsequent felony offense under Va. Code § 58.1-1017 a Class 5 felony.
- Option 3: Increase the misdemeanor offense under Va. Code § 58.1-1017 from a Class 2 misdemeanor to a Class 1 misdemeanor.
- Option 4: Increase the penalty for a second or subsequent misdemeanor offense, to either a Class 1 misdemeanor, or to a Class 6 felony, if Option 3 is adopted.

# Policy Considerations



**ISSUE 3:** Include the new cigarette trafficking statute, Va. Code § 58.1-1017.1, under Virginia's RICO statute, Va. Code § 18.2-513.

- Currently, possession of unstamped cigarettes already qualifies as a racketeering activity.

# Policy Considerations



**ISSUE 4:** Allow for the forfeiture of property used in connection with cigarette trafficking and cigarette tax evasion.

- Under existing law, Va. Code § 19.2-386.21, property that is used in connection with cigarettes that have counterfeit tax stamps is subject to forfeiture.

# Policy Considerations



## **ISSUE 5:** Allow localities to create local ordinances that allow for enforcement of Va. Code § 58.1-1017.1.

- Localities already have the authority to use local ordinances against defendants who fail to pay local cigarette taxes, pursuant to Va. Code § 58.1-3832.
- Allowing them to use local ordinances against smurfs might provide an incentive to vigilantly patrol for this frequently blatant criminal behavior.

# Policy Considerations



**ISSUE 6:** Make the possession of counterfeit cigarettes under Va. Code § 18.2-246.14 a crime, in addition to the current civil penalties.

-Under Va. Code § 59.1-92.13, knowing violations of Virginia's trademark statute are a Class 1 misdemeanor; possession of 100 or more identical counterfeit registered marks is a Class 6 felony.

# Policy Considerations



**ISSUE 7:** Virginia should consider increasing its efforts in the enforcement of illegal cigarette trafficking and allocate additional resources to agencies responsible for investigations and enforcement.



# Policy Considerations



**ISSUE 8:** Ensure law enforcement receives training on the seriousness of illegal cigarette trafficking, methods that traffickers use, and how to proceed when they encounter these crimes.

- DCJS could help coordinate this training.

# Policy Considerations



**ISSUE 9:** Organize a one day conference for key stakeholders to raise awareness of the issue of cigarette trafficking.

- Include local law enforcement, the VSP, Commonwealth's Attorneys, ATF, the Office of the Attorney General of Virginia, DCJS, NVCTB, Tobacco Commission, Va. Dept. of Taxation, the judiciary, manufacturers, wholesalers, and retail merchants.
- A general meeting of key stakeholders could provide valuable ideas and strategies on how coordination and cooperation can help combat this emerging criminal problem.

# Policy Considerations



**ISSUE 10:** Encourage the Virginia State Police to consider developing an information sharing system, accessible only to law enforcement, that would allow for the collecting of raw data and criminal intelligence on cigarette traffickers.

- This system could be made available to federal law enforcement and law enforcement in other states, in order to better combat organized crime.
- Crime Commission staff could assist and/or facilitate any necessary planning meetings.

# Policy Considerations



**ISSUE 11:** The Virginia Department of Taxation should consider collecting information on which retailers in Virginia sell tobacco products.

- This information would assist the Department of Taxation with their retail store site inspections.

# Policy Considerations



**ISSUE 12:** Encourage the Virginia Department of Taxation and the Office of the Attorney General of Virginia to consider requiring, or allowing the option of, electronic filing of all mandatory reports by cigarette wholesalers.

- Currently, forms are on paper and are delivered by mail.
- Electronic filing of these records could reduce long-term costs to wholesalers, increase the amount of information they provide without significant additional costs, and might increase tax compliance.



## **Discussion**

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