

Approved May 11, 2002  
Date

MINUTES OF THE HOUSE COMMITTEE ON TAXATION

The meeting was called to order by Chairman Edmonds at 9:00 a.m. on May 2, 2002 in Room 519-S of the Capitol.

All members were present except: Representative Mays, excused  
Representative Osborne, excused

Committee staff present: Chris Courtwright, Legislative Research Department  
April Holman, Legislative Research Department  
Don Hayward, Revisor  
Winnie Crapson, Secretary

Conferrees appearing before the Committee:  
Representative Merrick  
Sally Finney, Kansas Health Care Access Coalition  
Mark Tallman, Kansas Association of School Boards'  
Stephanie Sharp, American Cancer Society  
Jerry Slaughter, Kansas Medical Society  
Ron Hein, R. J. Reynolds Tobacco Company  
Tom Palace, Petroleum Marketers and Convenience Store Association  
Karl Peterjohn, Kansas Taxpayers Network  
Marlee Carpenter, Kansas Association of Commerce and Industry

Others Attending: See attached list.

**Hearing was opened on**

**HB 3038 - Cigarette and tobacco product tax rate increase.**

Chairman Edmonds explained that **HB 3038** would increase tax on cigarettes from 24 cents to \$1.00 with corresponding increases in tax on tobacco products.

Sally Finney presented testimony in support on behalf of the Kansas Health Care Access Coalition (Attachment #1). She said there are now 124 organizations which have come together in the Coalition specifically for the purpose of supporting a sales tax increase on cigarettes of not less than 65 cents. Her testimony included a list of those members. The testimony addresses questions raised such as regressivity, cross-border sales, and reduction in smoking and increasing revenue. Her testimony included the poll findings indicating that support for a significant cigarette tax increase is broad based and cuts across party lines with 72% of all voters in Kansas in support. She provided with the testimony editorials by Bob Johnson in the Iola Register and by Tom Bell in the Salina Journal.

In response to questions Ms. Finney said Kansas last raised its excise tax on cigarettes in 1985 and that a number of other states are considering increases, including Missouri and Oklahoma, and a measure passed in Nebraska last month rising their cigarette excise tax by 30 cents. She said that Kansas City, Missouri has more excise tax than Kansas when considering taxes are levied by the state, by Jackson County, and by the City of Kansas City, Missouri. She said that because the tax is assessed at the distributor level, providers of cigarettes through mail order and the internet are required by federal law to register with states so tax can be levied at the distributor level. Tax is paid on cigarettes sold on Reservations although they may choose not to pass that cost on to their customers.

When asked if she believed this increase in tax on cigarettes would result in reduction in smoking, she said it would contribute in a comprehensive program to discourage smoking.

## CONTINUATION SHEET

Mark Tallman presented testimony in support of **HB 3038** on behalf of the Kansas Association of School Boards and the School Finance Coalition (Attachment #2), which also included testimony in support of **HB 3039**. The organizations have not proposed a specific tax proposal but believe both measures being heard in the Committee today are acceptable as part of a revenue plan to fund the state's priority programs. The testimony set forth goals they believe the revenue plan enacted by the Legislature must meet. They believe considering inflation and rising costs for health and property insurance a flat budget does not hold education "harmless" and that without a revenue measure that meets the criteria outlined the quality of education will be at risk, local property taxes will increase, and families will face higher student fees and fewer services. They believe that Kansans have enjoyed significant cuts in both state and federal taxes in recent years and are willing to pay more to support their schools. Mr. Tallman responded to questions.

Stephanie Sharp presented testimony in support of **HB 3038** on behalf of the American Cancer Society (Attachment #3). She presented information on tobacco use and cancer and said since 1985, the last time Kansas increased the tax, every other state in the Union has increased their taxes with the exception of the eight primary tobacco-producing states and Kansas.

Jerry Slaughter appeared on behalf of the Kansas Medical Society in support of **HB 3038**.

Ron Hein presented testimony in opposition to **HB 3038** on behalf of R. J. Reynolds Tobacco Company (Attachment #4) because they believe it would hurt customers and retailers alike. He said that since the Kansas excise tax was last increased Kansas smokers have seen significant increases in the cost of cigarettes due to federal excise tax increases and as a result of the Master Settlement Agreement between the states and the tobacco industry. His testimony outlined the factors that impact the cost of cigarettes. Mr. Hein said tobacco sales have an especially magnified impact on smaller establishments such as convenience stores because cigarette sales in such stores accounted for nearly 30% of merchandise sales and that over 50% of all tobacco products are sold through convenience stores nationwide. The cross-border threat was also addressed in the testimony.

Tom Palace presented testimony on behalf of the Petroleum Marketers and Convenience Store Association in opposition to **HB 3038** (Attachment #5). He said the increase proposed would change buying habits and surrounding states and internet sales may be the benefactors at the expense of Kansas convenience stores.

Karl Peterjohn provided a statement in opposition on behalf of the Kansas Taxpayers Network (Attachment #6), saying the Network's opposition to raising taxes is constant, consistent and continuing; that **HB 3038** proposes another large increase in the cigarette excise tax as the latest effort to enact this type of tax and referred members of the Committee to his earlier testimony stating that the bill should be labeled "Western Missouri Retail Development Act of 2002." They believe there will be huge unintended negative consequences by creating a larger disparity between Kansas tax rates and our neighbors.

Hearing on **HB 3038** was closed.

**Hearing was opened on HB 3039 - Sales tax rate.**

Chairman Edmonds explained the bill would increase sales tax from 4.9 to 5 on a permanent basis and to 5.25 for one year.

Marlee Carpenter presented testimony on behalf of the Kansas Association of Commerce and Industry (Attachment #7) taking a neutral position on the bill but noting the desirability of providing allowances for administrative costs.

Mark Tallman testified in support of **HB 3039** on behalf of the Kansas Association of School Boards and the School Finance Coalition. He referred the Committee to his earlier comments and the testimony provided in Attachment #2.

CONTINUATION SHEET

Karl Peterjohn presented testimony in opposition to **HB 3039** on behalf of the Kansas Taxpayers Network (Attachment #8). He said this was another large increase in the sales tax this June with a partial roll back that may or may not take place next June and that only Nebraska among our neighboring states imposes as high a state rate on sales as 5 percent and Nebraska exempts grocery/food purchases from its sales tax.

Hearing on **HB 3039** was closed.

The Committee adjourned at 10:15. No schedule is set for a future meeting.

## GUEST LIST

DATE May 2, 2002

NAME	REPRESENTING
Marlee Carpenter	KCCI
Cindy Shaw	SMCA
Hilson Krueger	Western Wireless
Larry R Buzze	LKM
M Whitaker	KBWA
Leslie Kaufman	KFB
Christi Stewart	KMCA
Deann Williams	KMCA
Berake Koch	Wichita Area Chamber
Dodie Wellhead Johnson	Patrick Hurley & Co.
Wes Beal	TFKC
Jim Yonally	Verizon Wireless
Whitney Jauron	Smokers Tobacco Council Inc.
Kelly Tracy	Ka. Health Care Access Coalition
Christy Caldwell	Topeka Chamber of Comm.
John Frelund	Boeing
Bob Harder	WMC-KS
Paul M. Whib	Assoc. Committee of Ms.
Shanty Kennedy	Consortium
Karl Petavida	Ka. Taxpayers Network
Maryanne Kelleher	USKI
Ann Snikes	DOB
Bill Snick	S.M. Schools
Judy Keller	American Lung Assn.



# KANSAS HEALTH CARE ACCESS COALITION

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KANSAS MEDICAL SOCIETY  
KANSAS HOSPITAL ASSOCIATION  
KANSAS PUBLIC HEALTH ASSOCIATION  
AMERICAN HEART ASSOCIATION  
AMERICAN CANCER SOCIETY  
TOBACCO FREE KANSAS COALITION  
AMERICAN LUNG ASSOCIATION  
KANSAS STATE NURSES' ASSOCIATION  
AMERICAN ACADEMY OF PEDIATRICIANS  
KANSAS ACTION FOR CHILDREN  
ASSOCIATION OF COMMUNITY MENTAL HEALTH CENTERS OF KANSAS  
KANSAS FOR ADDICTION PREVENTION  
DCCCA  
CATHOLIC COMMUNITY SERVICES  
KANSAS ACADEMY OF FAMILY PHYSICIANS  
KANSAS ASSOCIATION OF LOCAL HEALTH DEPARTMENTS  
KANSAS ASSOCIATION FOR THE MEDICALLY UNDERSERVED  
KANSAS CHAPTER OF NATIONAL ASSOCIATION OF SOCIAL WORKERS  
KANSAS PHARMACISTS ASSOCIATION  
CHRIST THE KING CATHOLIC CHURCH  
KANSAS ECUMENICAL MINISTRIES  
KANSAS SMOKELESS KIDS INITIATIVE  
PUBLIC ASSISTANCE COALITION OF KANSAS  
UNITED METHODIST CHURCH OF KANSAS  
KANSAS DENTAL ASSOCIATION  
TOPEKA CENTER FOR PEACE AND JUSTICE

To: Members of the House Committee on Taxation  
From: Sally Finney  
Re: HB 3038  
Date: May 2, 2002

Chairman Edmonds and members of the committee, I am Sally Finney, Executive Director of the Kansas Public Health Association. I appear before you today as spokesperson for the Kansas Health Care Access Coalition to ask you to support HB 3038, a proposal increasing the excise tax on cigarettes by 76 cents per pack.

The Kansas Health Care Access Coalition is comprised of 124 organizations that deal with health care and concerns related to the well-being of Kansans. A list of coalition members is attached to the information packet that accompanies my testimony.

While we are a diverse group, we have a common bond when it comes to the benefits of reducing cigarette consumption in Kansas. Both overwhelming statistical evidence, and common sense, tell us all that ours will be a safer, cleaner, healthier state if cigarette consumption is decreased.

Cigarettes cost Kansas, both in human terms and in financial ones. The Kansas Health Care Access Coalition believes this is a problem we can no longer afford to ignore.

**Increasing the tax on cigarettes makes good health policy.** Some of the projected health benefits from increasing the state cigarette tax by 76 cents include:

- Fewer packs of cigarettes smoked each year: 19.8 million.
- Number of current adult smokers in Kansas who will quit: 19,100.
- Number of kids alive today who would not become smokers: 22,000.
- Number of kids alive today saved from smoking-caused death: 7,100.

**Increasing the tax on cigarettes makes good fiscal policy.** In 2001, the state-paid portion of Medicaid costs attributable to smoking was \$68.9 million (an increase of 138% since 1993). Annual health care expenditures

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in Kansas directly related to tobacco use exceed \$630 million. These figures exclude lost revenue from sick smokers who are unable to work and related costs to employers for such expenses as decreased productivity from absenteeism due to illness and increased health insurance for workers.

The projected \$126 million in new revenue that will result from passage of HB 3038 will give you and the Governor options as you struggle to deal with decisions about state spending, decisions that will directly affect the ability of the state to serve its citizens. In addition to helping you deal with our state's current fiscal concerns, increasing the cigarette tax would mean

- 5-year healthcare savings from fewer smoking-affected pregnancies and births: \$4.7 million.
- 5-year healthcare savings from fewer smoking-caused heart attacks and strokes: \$6.5 million.
- Long-term healthcare savings in Kansas from declines in youth and adult smokers: \$424.0 million.

Cigarettes, when used as directed, kill. They cost the Kansas economy, and each year they cost nearly 5,000 Kansans their lives. Raising the tax on cigarettes does make sense. The Kansas Health Care Access Coalition asks you to support HB 3038.

# KANSAS HEALTH CARE ACCESS COALITION

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## Cross Border Sales

Allegation: **Raising our excise tax will cause Kansans to “flock” to neighboring states or engage in smuggling to avoid paying taxes in Kansas.**

### The Facts

- With the exception of Colorado, all of Kansas’ neighboring states are seriously considering excise tax increase because of budget situations similar to that of Kansas. *Source: Tobacco Free Kansas Coalition*
- Missouri not only levies a state excise tax, but some local jurisdictions also levy a city and county tax. In Kansas City, Missouri the total city, county and state excise tax on cigarettes exceeds that of the Kansas tax. *Source: Jordan Griffin, Financial Manager, Revenue Division, Kansas City, Missouri Finance Department*
- Informal cross-border purchases by consumers and small-time smugglers account for only about one percent of all cigarette purchases. U.S. smuggling studies show that organized cigarette smuggling (with wholesaler or retailer participation) accounts for only three to five percent of all cigarettes purchased in the United States. *Source: See, e.g., Yurekli, A. & P. Zhang, "The Impact of Clean Indoor-Air Laws and Cigarette Smuggling on Demand for Cigarettes: An Empirical Model," Health Economics 9:159-170 (2000); Thursby, JG & MC Thursby, "Interstate Cigarette Bootlegging: Extent, Revenue Losses, and Effects of Federal Intervention," unpublished manuscript (January 1998) [earlier version published as National Bureau of Economic Research report; see, also, Thursby, M., et al., "Smuggling, Camouflaging, and Market Structure," Quarterly Journal of Economics, 106: 789-814 (August 1991)]; Saba, RP, et al., "The Demand for Cigarette Smuggling," Economic Inquiry 33: 189-202 (April 1995). See, e.g., Thursby, Jensen, Thursby (August 1991). See, e.g., Fleenor, P., "The Effect of Excise Tax Differentials on the Interstate Smuggling and Cross-Border Sales of Cigarettes in the United States," The Tax Foundation (October 1996).*
- Current Kansas law prohibits bringing into Kansas more than 20 packages of cigarettes without the appropriate tax stamps. *Source KSA 79-3323*

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# KANSAS HEALTH CARE ACCESS COALITION

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## Mail Order and Internet Sales

Allegation: **If Kansas increases its excise tax on cigarettes then smokers will resort to mail order and Internet sales to purchase cigarettes and avoid paying state taxes.**

The Facts:

- Federal law requires businesses or individuals selling cigarettes to out-of-state customers to register with each state in which they are conducting business and report each month to the state revenue officials the name, address, brand of cigarette and quantity sold to each customer within that state for the preceding month.

*Source: US Code Title 15, Chapter 10A, Sections 375-378*

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# KANSAS HEALTH CARE ACCESS COALITION

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## Military and Native American Sales

Allegation: **Raising our excise tax will cause people to go to military installations and Native-American "smoke shops" to avoid paying the increased excise tax.**

### The Facts:

- Only military personnel with appropriate military identification can purchase cigarettes or other tobacco products on a military installation. *Source: Janet Wray, Public Information Officer, Fort Leavenworth, KS & Christie Vanover, Deputy Media Relations Officer, Fort Riley, KS.*
- The Department of Defense is making tobacco products less accessible at commissaries and exchanges. Cigarettes used to be much less expensive at these stores than off base. The Department of Defense has since succeeded in having the prices of tobacco products raised at commissaries and exchanges to make smoking less attractive. *Source: Lt. Col Wayne Talcot of the Air Force Medical Operations Agency in an interview with the Armed Forces Information Service, November 2001.*
- Excise taxes placed on cigarettes are imposed on the wholesaler, therefore, retailers - even those on Native-American tribal land - must either pass this tax onto their customers or accept lower profit margins
- The United States Supreme Court has held that state tobacco taxes cannot be imposed on tribal members making purchases on tribal land without agreement between the tribes and states. Their ruling did state that state taxes on sales to non-tribal members must be collected and remitted to the state. *Source: Oklahoma Tax Commission v. Citizen Band of Potawatomi, 498 U.S. 505 (1991)*

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## The Canadian Experience

Allegation: Tobacco industry supporters suggest that the Canadian experience with increased excise taxes gives proof that higher excise taxes lead to smuggling.

### The Facts:

- Smuggling did increase in Canada in the early 90's, but the smuggling was part of an extensive organized effort by the tobacco industry to undercut the excise tax imposed by Canada.
- R.J. Reynolds Canadian affiliate, Northern Brands and its former President, Les Thompson, have each pleaded guilty to charges of being involved in illegal smuggling. Thompson is currently in prison because of his role in the organized smuggling operation. *Source: CBS, 60 Minutes II, "Tobacco's Other Secret" (January 18, 2000). Marsden (December 18, 1999).*
- Thompson, in an interview with 60 Minutes II, stated that R.J. Reynolds set up its Canadian affiliate, Northern Brands, expressly for the purpose of smuggling cigarettes into Canada and was fully aware of the affiliate's effort to encourage and support the smuggling. *Source: CBS, 60 Minutes II, "Tobacco's Other Secret" (January 18, 2000). Marsden (December 18, 1999).*
- R.J. Reynold's Thompson indicated that during the time of the smuggling operation in Canada, 60-percent of RJR's Canadian business was from smuggled cigarettes. *Source: 60 Minutes II (January 18, 2000). See also, Marsden (December 18, 1999).*
- The Canadian smuggling operation was not limited to R.J. Reynolds. Brown & Williamson sales managers pleaded guilty to the charge of aiding smugglers who were illegally bringing cigarettes into Canada by supplying the smugglers with untaxed cigarettes from a bonded B&W warehouse in Alabama. *Source: Dow Jones News Service, "Ex-Brown and Williamson Manager Gets Probation for Smuggling" (October 15, 1997).*

Evidence was also uncovered that a subsidiary of Philip Morris and a subsidiary of British American Tobacco were also involved with Canadian smuggling. *Source: Marsden (December 18, 1999). See, also, Thompson, F., "Imperial Tobacco, Imasco, and the Smuggling of Cigarettes into Canada," Non-Smokers' Rights Association (Canada) (January 28, 2000).*

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KANSAS  
ASSOCIATION



OF  
SCHOOL  
BOARDS

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Testimony on  
**HB 3038 (Cigarette Tax Increase)**  
**HB 3039 (Sales Tax Increase)**  
Before the  
House Committee on Taxation

by

Mark Tallman, Assistant Executive Director/Advocacy  
Kansas Association of School Boards  
Representing the School Finance Coalition

May 2, 2002

Mr. Chairman, Members of the Committee:

I have included comments on both measures before you today in this statement. Our organizations have not proposed a specific tax proposal, but we believe both measures before you today are acceptable as part of a revenue plan to fund the state's priority programs. We believe the Legislature must enact a revenue plan that meets the following goals:

- It must provide enough revenue to fund at least the current level of educational funding plus the minimal \$20 base increase recommended by Governor Graves.
- It must provide on-going revenue to ensure adequate funding for future educational needs.
- It must maintain an ending balance that meets the state's cash flow requirements, to avoid delays in making school aid payments, such as experienced this year.

Based on these objectives, we support these bills as part of the revenue package the state will need, but we do not believe these measures alone will be adequate.

If the target for raising revenue is the conference committee report on the budget, that budget provides no increase in the base budget for school districts. While that budget does not cut the base, flat funding does not "hold harmless" schools. With inflation estimated at 2.5 percent and many school districts expenditures such as health and property insurance rising far more rapidly than the rate of inflation, a budget that "holds harmless" education is not harmless. Even if the base is unchanged or raised slightly, many school districts will be forced to reduce staff, cut programs, raise property taxes – or a combination of all three.

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Our second point is that the revenue plan should provide on-going support for education and other state priority programs. The additional revenue raised by the sales tax increase contained in HB 3039 will fall by nearly approximately \$80 million if the rate is reduced in FY 2004. We believe this will make any increase in school funding extremely difficult next year, as well. In fact, it suggests that the 2003 Legislature will likely face the same budget difficulties it currently confronts. This problem will be compounded if the state needs to rebuild ending balances.

The ending balance is important for school districts for several reasons. First, if state balances are too low, the state can have difficulty making aid payments to school districts on time, as has happened several times this year. Second, if state revenues fall below projections, or if unanticipated expenditures occur, mid-year cuts could be required. School budgets would almost certainly have been reduced during the current year if the state had not had an 8.3 percent balance last June 30. Third, using balances to pay current expenses is "one time" money that must be replaced. Even if the economy rebounds, the growth in tax revenues would likely be used to replace those balances, and little or no increase would be available to help districts meet rising costs. If the economy doesn't rebound, education would again face the prospect of major reductions.

In conclusion, we support these revenue measures, but we believe that meeting the needs of public education will require a larger tax increase than these bills alone. Without a revenue measure that meets the criteria outlined above, the quality of education will be at risk, local property taxes will increase, and families will face higher student fees and fewer services. Jobs will be lost, schools will be closed and communities will suffer. In recent years, Kansans have enjoyed significant cuts in both state and federal taxes. They are willing to pay more to support their schools, their children and their future.

Thank you for your consideration of our position on these measures.

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May 2, 2002

**Testimony in Support of House Bill 3038 to the House Taxation Committee**

Chairman Edmonds and Members of the Committee:

As the Government Relations Director for the American Cancer Society, I represent more than 270,000 volunteers, supporters, and staff across the state of Kansas. Also, as a member of the Kansas Health Care Access Coalition, your American Cancer Society supports Governor Graves \$0.65 cigarette excise tax increase proposal, and considers it to be the "floor" for this tax. Thus, we applaud your courageous efforts and render our whole-hearted support for House Bill 3038 and its provision to increase the state cigarette tax by \$0.76.

We unite with more than 40 health-interest organizations that have joined forces to form the Kansas Health Care Access Coalition in the battle to save the lives and lungs of Kansas children. Since 1985 - Kansas last increase - every other state in the Union has increased their cigarette tax, EXCEPT the eight primary tobacco-producing states, AND Kansas. Is this the company we want to keep? Kansas children deserve better.

The link between tobacco use and cancer is no secret:

- 1 in 3 cancer deaths are tobacco-related;
- Tobacco causes nearly 90 percent of lung cancers;
- Lung cancer is not the sole cancer risk for smokers. Tobacco use is a risk factor for nearly every other cancer – colon, breast, cervical, prostate, pancreatic, kidney, liver, throat, and the list goes on.

Smoking kills thousands every day - parents and grandparents that miss out on valuable years, because they were chained by an addiction that hooked them as children. Let's not leave that fate to the next generation of Kansans. A \$0.65 cigarette tax increase will keep 19,000 Kansas children from ever becoming smokers, and will encourage more than 16,000 adult smokers to quit! Imagine the impact of a larger increase...

Not only can a \$0.76 increase in the cigarette tax save children and parents from addiction, but the significant revenue generated by this tax will enable the state of Kansas to maintain the services and quality of life we have all come to expect as Kansans: state-of-the-art health care facilities and care, quality schools, safe roads, and low crime.

American Cancer Society advocates in your districts have contacted you to support this tax. They expect you to be their voice. Will you speak for them? Please support HB 3038.

Stephanie Sharp, Government Relations Director

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**Testimony re: HB 3038  
House Taxation Committee  
Presented by Ronald R. Hein  
on behalf of  
R. J. Reynolds Tobacco Company  
May 2, 2002**

Mr. Chairman, Members of the Committee:

RJR opposes HB 3038, which would increase the Kansas cigarette tax 76¢ from 24¢ to \$1.00 per pack, because it would hurt consumers and retailers alike. This is a 316% increase

**Current tax rate and past tax increases**

Supporters of increasing the cigarette tax in Kansas have cited frequently that the current state excise tax on cigarettes has not been raised in a number of years. However, this does not tell the entire story.

Since the Kansas excise tax was last increased, Kansas smokers have seen significant increases in the cost of cigarettes, some of that increase goes to the federal government because of excise tax increases, much of that increase goes to the state of Kansas as a result of the Master Settlement Agreement (MSA) between the state attorneys general and the tobacco industry, and smokers pay increased sales tax on the increases in the cost of cigarettes.

The federal tax on smokers has increased substantially over the past 15 years. Since 2000, federal taxes on a pack of cigarettes have increased 62.5%, including an additional federal tax of 5 cents beginning January 1, 2002.

Under the MSA, Kansas will collect \$1.6 billion over the next 25 years from the nations' largest cigarette manufacturers. (Although payments are calculated over a 25-year time-frame, in fact they go on for perpetuity.) This means that Kansas smokers will pay approximately \$1.6 billion over the next 25 years to the state of Kansas in addition to the excise taxes and sales taxes they are paying on cigarettes.

Kansas will receive approximately \$65 million per year in annual MSA payments. This amounts to a payment to Kansas that is more than the amount that Kansas derives from its 24¢ per pack cigarette tax.

Lastly, Kansas imposes a sales tax on cigarette sales. The 4.9% state sales tax is also imposed on the excise taxes and MSA payments built into the cost of a pack of cigarettes. Since the

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cost of a pack has gone up substantially as a result of the MSA, Kansas is taxing smokers much more with the additional sales tax. Nationally, from 1998 to 2001, the average price per pack rose from \$2.04 to \$3.28. If this national average was also true in Kansas, the amount of state sales tax imposed on smokers would have increased greater than 50% during that three-year period.

All together Kansas smokers are financing federal and state governments to the tune of \$1.33 per pack. The typical Kansas smoker now pays about \$700 in total tobacco revenue per smoker, larger than the average income liability for the bottom half of federal income tax filers (about \$540 in 1998.) After a 76¢ Kansas tax hike, the total tax burden on the smoker would rise to a stupendous \$2.09 per pack. A Kansas smoker would be paying well over \$1,000 per year.

**The argument that Kansas smokers have not had a tax increase in years is simply not accurate, as seen by the above information.**

**Effect on Kansas Retailers.**

Kansas retailers should also be concerned. The new \$1.00 tax would be 56% higher than the new rate in Nebraska (was 34¢, increased this year to 64¢ with a two-year sunset clause), **almost six times** the existing Missouri tax (17¢), **five times** the tax in Colorado (20¢), and **more than four times** the Oklahoma rate (23¢). If the proposal of increasing the cigarette tax to a total of \$1.00 were to pass, that would mean Kansans could save significant money simply by crossing borders. Colorado also does not impose a sales tax on cigarettes, making the differential even higher.

Cigarette purchasing patterns have changed dramatically since 1989. High-tax states have seen tax reported sales plunge, while low-tax states have seen a corresponding increase.

With low tax Missouri, Colorado and Oklahoma on its borders, Kansas' retailers could confront a competitive challenge. Nearly 25% of Kansas' population lives in the greater Kansas City area, which borders Missouri. Kansas consumers could save as much as \$5.90 per carton purchasing in Missouri, assuming their existing tax rate. Some of these margins come close or exceed the Advisory Commission on Intergovernmental Relation's bootleg "flashpoint" of \$3.80 per carton. Tax differences above the "flashpoint" are likely to encourage serious investments in cigarette smuggling. Kansas retailers, and ultimately state law enforcement budgets, would be vulnerable to smuggling.

Tobacco products are sold in many types of stores including convenience stores, gas stations, supermarkets, tobacco stores, drug and proprietary stores. According to a 1998 study by the American Economics Group (AEG), nearly 11,000 jobs were directly and indirectly created due to such activities.



Tobacco sales have an especially magnified impact on smaller establishments. This is because cigarette sales comprise such a large share of their sales. In 2000, The National Association of Convenience Stores reported that tobacco sales in such stores accounted for nearly 30% of merchandise sales. Over 50% of all tobacco products are sold through convenience stores nationwide.

**Loss in Cigarette Sales Volume** – Assuming no changes in tax rates of surrounding states, it is projected that a 65¢ per pack tax increase will reduce Kansas cigarette sales by approximately 24%. I do not have a specific projection on the impact of the 76 cent increase for this testimony. Most of this would be due to lost sales to low-tax states and zones.

**Loss in Retail Sales** - The gross retail value of lost cigarette sales for a 65 cent increase would be approximately \$30 million (10 million packs evaluated at a final retail price of \$3.00 per pack). Sundry product sales, or products normally bought in conjunction with tobacco products, would fall by about \$12 million (based on past estimates of this phenomenon by Price Waterhouse). A 76 cent increase would increase the numbers for lost cigarette and sundry sales.

**Lost Jobs** - It is estimated that nearly 400 Kansas jobs would be lost as a result of a 65¢ tax increase. Once again, the affect of a 76¢ increase would be worse.

It is estimated that a 65¢ per pack tax hike will lead to about a \$152 million reduction in cigarette sales for Kansas' businesses. Sundry product losses would be about \$46 million. Again, a 76¢ increase will be worse. It is obvious that Kansas businesses will lose revenue, and the state will lose corresponding excise and sales taxes from the cigarettes and other sundry items.

**The Cross Border Threat**

Cigarette purchasing patterns have changed dramatically due to more than 70 state cigarette tax increases since 1989. High-tax states have seen tax reported sales plunge, while low-tax states have seen a corresponding increase. The Tax Foundation examined this shift in a 1996 study, The Effect of Excise Tax Differentials on Smuggling and Cross Border Cigarette Sales. They discovered that tax differentials between high and low-tax states were creating substantial increases in both casual cross-border purchases and the organized smuggling of cigarettes. In a subsequent study, the Tax Foundation estimated that cross-border sales represented nearly 14% of total U.S. sales in 1997.

The Tax Foundation noted that the following high-tax block of states -- California, Massachusetts, Michigan, and New York -- with an average tax of 73¢ per pack, sell fewer cigarettes than the following low-tax states -- Indiana, Kentucky, Missouri, New

Hampshire, North Carolina, Tennessee, and Virginia -- with an average tax of 13¢ per pack. Yet the four high-tax states have a population (65.4 million) nearly double that of the low-tax states (34.4 million).

In 1995, for the first time in history, the low-tax block sold more cigarettes (4.4 billion packs) than the high-tax block (4.3 billion packs). Since then, the gap has widened. In FY 2000, tax-reported sales in the low-tax block were 20% greater than such sales in the high-tax block. Kansas could easily be swept up in the cigarette smuggling epidemic that now plagues some other states.

Consider the case of Michigan. After it increased its cigarette tax from 25¢ to 75¢ per pack in May of 1994, annual Michigan cigarette sales nose-dived by 27 percent. On the other hand, annual cigarette sales went up by 8 percent in Kentucky, 14 percent in South Carolina, 12 percent in Indiana, 7 percent in Tennessee, 6 percent in North Carolina, 4 percent in Missouri, and 2 percent in Ohio. The sales volume gain in the low-tax states more than matched the 200 million-pack loss in Michigan.

In the words of Robert Manes, head of the Michigan State Police Treasury Enforcement Division, “[E]fforts to get around the tax increase are a growing problem. With the amount of money that can be made now, everybody who has an avenue is getting into it.” (Associated Press, December 13, 1994).

More recent cross border episodes include:

New York - The Empire State cigarette tax increased by 55¢ (from 56¢ to \$1.11 per pack) on March 1, 2000. During the following 12 months, New York tax-paid cigarette volume packs nose-dived by 24%. Neighboring Vermont (44¢) and Pennsylvania (31¢) have seen their sales volume rise over this time. It has been estimated that contraband and cross border cigarette sales now take nearly 25% of the New York market.

California – The Golden State’s cigarette tax increased by 50¢ (from 37¢ to 87¢) on January 1, 1999. California tax paid cigarette sales volume has fallen by nearly 25%. California State officials now estimate that cigarette excise tax losses due to tax evasion exceed \$150 million per year. This means that tax-evading sales take more than 12% of the entire California cigarette market. According to state tax officials. “illegal and untaxed sales have mushroomed.”<sup>1</sup> According to state officials, counterfeit stamps can be found throughout the state and appear to be a growing problem. Internet sales have grown as well, and are now estimated to be beyond \$60 million per year in California.

<sup>1</sup> “State Officials Fear Big Drop in Tariff Revenue,” *San Diego Times-Union*, April 19, 2001.

House Taxation Committee  
HB 3038  
May 2, 2002

**Regressivity**

A recent study by the Barents Group of KPMG Peat Marwick shows that cigarette taxes are incredibly regressive, extracting a far greater percentage of income from modest wage earners compared to those with high incomes.

Barents looked at U.S. families in the bottom half of the income distribution, those earning approximately \$30,000 a year or less. While this group represents roughly 50% of all households in the country, it earns only 16% of all income generated. This group pays about 15.3% of all federal income and FICA taxes, but pays over **47% of all tobacco taxes.**

Barents found that while most excise taxes are regressive, tobacco excise taxes are the most regressive of all. While the bottom half of U.S. households only reaped 16% of all income, they paid 47% of tobacco taxes, 17% of wine taxes, 30% of gas taxes, 30% of distilled spirits taxes and 34% of beer taxes. Clearly, the Kansas cigarette tax hike will harm those with modest incomes the most.

Thank you very much for permitting me to testify and I will yield for any questions.

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MEMO TO: House Taxation Committee  
FROM: Thomas M. Palace, Executive Director of the Petroleum Marketers and  
Convenience Store Association of Kansas  
DATE: May 2, 2002  
RE: HB 3038

Mr. Chairman and members of the House Taxation Committee: My name is Tom Palace and I am the Executive Director of the Petroleum Marketers and Convenience Store Association of Kansas (PMCA), a statewide trade association that represents over 360 independent petroleum marketers and convenience stores throughout Kansas.

I appreciate the opportunity to appear before you today in opposition to HB 3038.

Convenience store owners in Kansas who compete with bordering states will be at a tremendous competitive disadvantage if HB 3038 were to become law. It is interesting to note that although tobacco has been deemed bad, the state of Kansas and the convenience store industry have a common bond with tobacco. Both rely on the revenues from the sale of cigarettes to meet budget demands. Smokers have been hit hard over the past 3-4 years, seeing tremendous price increases largely due to the Master Settlement Agreement (MSA). Today's 24 cent per pack tax already puts Kansas above 3 of the 4 bordering states; Missouri 17 cents; Colorado 20 cents; Oklahoma 23 cents and Nebraska 34 cents. The increase will negatively impact every tobacco retailer on Kansas borders by pushing the smoking consumer into neighboring states.

Tobacco sales and gas sales are the "bread and butter" of the convenience store industry. Consumers usually stop at a convenience store because service is quick, and the customer can be in and out of the store in under 5 minutes. Cigarette sales are an important product for convenience stores, not only because cigarette sales make up approximately 23% of gross sales, but also because these sales lead to other sales such as pop, coffee, sandwiches, etc. The increased price of cigarettes has the potential of changing peoples' buying patterns, thus reducing store revenues for all products sold in convenience stores....as well as sales tax for the State of Kansas.

Over the past few years tobacco increases have been proposed in the legislature as a way to STOP people from smoking. If this is true, how can the state rely on tobacco revenue to fund new government programs? How will the money the state receives from the MSA be impacted? I would assume the state will see a reduction should tobacco sales decline. Also, Internet sales have become a factor. It is a sure bet that with an increase in cigarette taxes, the consumer will be motivated to use the Internet in ever-increasing numbers to purchase tobacco products. As a note of interest I accessed the Internet to look for sites that sell tobacco products. I found 18 sites that sell tobacco at discounted prices. I checked further into two eastern Native American tribes on the Web site and discover the following enticements:

Petroleum Marketers and Convenience Store Association of Kansas  
201 NW Highway 24 • Suite 320 • PO Box 8479  
Topeka, KS 66608-0479  
785-233-9655 Fax: 785-354-4374

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**“We have regulatory advantages that allow us to sell cigarettes at discounted prices.”**

And also -

**“CigaretteExpress.com does not report any sales activity to any State taxing authority and is not required to do so.”**

SenecaSmokes.com -

**“SenecaSmokes.com/Long Trails DOES NOT report to ANY state taxation or tobacco department.”**

Clearly smokers have options when it comes to purchasing cigarettes. As I mentioned earlier, smokers who have been hit hard with price increases are accustomed to making decisions as to what brand they will buy because of the cost, and where they can find the best price. The tax increase provided in HB 3038 will surely change buying habits once again. And it appears the surrounding states and the Internet may be the benefactors.

Mr. Chairman, competition in the convenience store industry is fierce. Add a 76 cent tax increase on cigarettes, and not only will the retail marketers be affected, but the state will lose revenue as well.

Thank you.

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**ANOTHER TOBACCO TAX BILL OPPOSED**

KTN's opposition to raising taxes is constant, consistent, and continuing. HB 3038 proposes another large increase in the cigarette excise tax that this organization opposes. Rather than repeating our testimony against this latest effort to enact this type of tax increase we will simply refer legislators to our earlier testimony against this bill that should be labeled the "Western Missouri Retail Development Act of 2002." This bill will have huge an unintended negative consequences by creating a large disparity between Kansas tax rates and our neighbors.

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# LEGISLATIVE TESTIMONY



*The Unified Voice of Business*

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HB 3039

May 2, 2002

## KANSAS CHAMBER OF COMMERCE AND INDUSTRY

Testimony Before the  
House Taxation Committee

by

Marlee Carpenter  
KCCI Director of Taxation

Mr. Chairman and members of the Committee:

I am Marlee Carpenter here on behalf of the Kansas Chamber of Commerce and Industry. The business community understands the grave budget situation you face as this session comes to an end. KCCI supports many state programs and hopes that legislators will hold these programs harmless. These programs include the 1999 Comprehensive Transportation Program, Economic Development funding, as well as K-12 and higher education.

The Kansas Chamber of Commerce and Industry (KCCI) is a statewide organization dedicated to the promotion of economic growth and job creation within Kansas, and to the protection and support of the private competitive enterprise system.

KCCI is comprised of more than 2,000 businesses which includes 200 local and regional chambers of commerce and trade organizations which represent over 161,000 business men and women. The organization represents both large and small employers in Kansas, with 48% of KCCI's members having less than 25 employees, and 78% having less than 100 employees. KCCI receives no government funding.

The KCCI Board of Directors establishes policies through the work of hundreds of the organization's members who make up its various committees. These policies are the guiding principles of the organization and translate into views such as those expressed here.

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Balancing these factors is difficult for any organization in these tight budget times. The reality of the situation has hit home with many business men and women and the need for additional state revenue seems imminent.

HB 3039, as written, is not a bill the Kansas Chamber supports. Sales tax increases are burdensome on retail operations in the state and presents challenge for retail businesses facing border state competition. KCCI's support for sales tax legislation hinges on state recognition of the contribution of retailers who collect and remit sales taxes, by permitting them to retain an administrative allowance. KCCI would be willing to support a modest increase in the state sales tax, up to .3%, that includes an administrative allowance for retailers.

Kansas retailers are required to collect and remit sales tax to the Kansas Department of Revenue without any compensation for their time or effort. Twenty-eight states including the District of Columbia provide an administrative allowance. KCCI knows that this measure could be costly, but a phase in of this type of compensation would be manageable.

I have attached to my testimony a list of sales tax and administrative allowance rates for 2001 and a list of other types of administrative allowances allowed by Kansas.

Thank you for your time and I will be happy to answer any questions.



## Types of Administrative Allowance allowed in Kansas

- **Kansas Use Tax.** Kansas provides the retailers of Missouri, Oklahoma, Nebraska and Colorado an allowance for the collection of Kansas' 4.9 percent use tax.
- **Transient Guest Tax.** Transient guest tax is collected by hotels and motels and forwarded to the Kansas Department of Revenue (KDOR) where it is processed and returned to the city or other taxing entity for use by the local Convention and Visitors Bureau. The amount returned to the local taxing jurisdiction is the amount "less 2% administrative fee" retained by KDOR.
- **Lottery Ticket Sales Commission.** Lottery ticket retailers are allowed to keep a commission off of the lottery tickets they sell.

**Motor Fuel Tax.** The distributor of motor fuels is allowed to retain 2.5% of the motor fuel tax for ordinary losses which may have resulted from physical loss while handling such motor-vehicle fuels.

## STATE SALES TAX RATES AND VENDOR DISCOUNTS

(January 1, 2001)

STATE	STATE SALES TAX RATE	RANK	VENDOR DISCOUNT	MAX/MIN
ALABAMA	4.0%	37	5.0%-2.0% (1)	
ALASKA		N/A		
ARIZONA (10)	5.0%	19	1.0%	\$10,000/year (max)
ARKANSAS	5.125%	18	2.0%	\$1,000/month (max)
CALIFORNIA (3)	5.75%	16	None	
COLORADO	2.9%	46	3.33% (4)	
CONNECTICUT	6.0%	8	None	
DELAWARE		N/A		
FLORIDA	6.0%	8	2.5%	\$30/report (max)
GEORGIA	4.0%	37	3.0%-0.5% (1)	
HAWAII	4.0%	37	None	
IDAHO	5.0%	19	None (5)	
ILLINOIS	6.25%	6	1.75%	\$5/year (min)
INDIANA (2)	5.0%	19	1.0%	
IOWA	5.0%	19	None	
KANSAS	4.90%	33	None	
KENTUCKY	6.0%	8	1.75%-1.0% (1)	
LOUISIANA	4.0%	37	1.1%(9)	
MAINE	5.0%	19	None (5)	
MARYLAND	5.0%	19	1.2%-0.9% (1)	
MASSACHUSETTS	5.0%	19	None	
MICHIGAN	6.0%	8	0.5% (6)	\$6/monh (min)
MINNESOTA	6.5%	3	None	
MISSISSIPPI	7.0%	1	2.0%	\$50/month (max)
MISSOURI	4.225%	36	2.0%	
MONTANA		N/A		
NEBRASKA	5.0%	19	2.5%-0.5% (1)	
NEVADA	6.5%	3	1.25%	
NEW HAMPSHIRE		N/A		
NEW JERSEY	6.0%	8	None	
NEW MEXICO	5.0%	19	None	
NEW YORK	4.0%	37	3.5%	\$85/month (max)
NORTH CAROLINA	4.0%	37	None	
NORTH DAKOTA	5.0%	19	1.5%	\$255/quarter (max)
OHIO	5.0%	19	0.75%	
OKLAHOMA	4.5%	35	2.25%	\$3,000/month (max)
OREGON		N/A		
PENNSYLVANIA	6.0%	8	1.0%	
RHODE ISLAND	7.0%	1	None	
SOUTH CAROLINA	5.0%	19	3.0%-2.0% (1)	\$3,000/year (max)
SOUTH DAKOTA	4.0%	37	None	
TENNESSEE	6.0%	8	2.0%-1.15% (1)	\$25/report (max)
TEXAS	6.25%	6	0.5% (7)	
UTAH	4.75%	34	1.5%	
VERMONT	5.0%	19	None (5)	
VIRGINIA (3)	3.5%	45	4.0%-2.0% (8)	
WASHINGTON	6.5%	3	None	
WEST VIRGINIA	6.0%	8	None	
WISCONSIN	5.0%	19	0.5%	
WYOMING	4.0%	37	None	
DIST. OF COLUMBIA	5.75%	16	1.0%	\$5,000/month (max)
U. S. MEDIAN	5.0%		2.0%-1.5% (1)	28 states allow vendor discounts

(1) In some states, the vendors' discount varies by the amount paid. In AL and SC, the larger discounts apply to the first \$100. In GA and NE, the larger discount applies to the first \$3,000. In TN and KY, the larger discounts apply to the first \$2,500 and \$1,000, while MD applies the larger discount to annual collections of \$6,000. The lower discounts apply to remaining collections above these amounts.

(2) Utilities are not permitted to take discount.

(3) Rate does not include a statewide local rate of 1.25% in CA and 1.0% in VA.

(4) Vendor discount applies to the state taxes collected. Discount for local option sales tax varies from 0% to 3.33%.

(5) Vendors are allowed to keep any excess collections prescribed under the bracket system.

(6) Vendor discount only applies to the first 4.0% of the tax.

(7) An additional discount of 1.25% applies for early payment.

(8) Discount varies; 4% of the first \$62,500, 3% of the amount to \$208,000, and 2% of the remainder.

(9) The vendors discount is scheduled to increase to 1.5% on July 1, 2001 in Louisiana.

(10) Tax rate scheduled to increase to 5.6% on 6/1/01.

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**ANOTHER SALES TAX BILL OPPOSED**

KTN's opposition to raising taxes is constant, consistent, and continuing. HB 3039 proposes another large increase in the sales tax this June with a partial roll back in the increase that may or may not take place next June.

HB 3039 would leave Kansans paying the highest state sales tax rate in our region even in the unlikely event that the partial roll back next year would actually occur. Only Nebraska among our neighboring states imposes as high a state rate on sales as 5 percent. Nebraska exempts grocery/food purchases from its sales tax.

HB 3039 would provide an additional incentive for Kansans to avoid the sales tax. This bill would aggravate the significant disparity between the state sales tax rate in Kansas and the state rate in Missouri.

Consumers in border areas will vote with their feet and the projected tax revenue growth will not meet projections based on static revenue growth forecasts.

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