

**Testimony in Opposition to S.B. 233
Kansas Senate Assessment and Taxation Committee
March 24, 2015**

Thank you, Chairman Donovan, Vice Chair Tyson and members of the Senate Assessment and Taxation Committee. My name is Bill Keip and I am a consultant to Reynolds American Services Company. I will limit my comments to the proposed cigarette excise tax rate increase (similar comments apply to Other Tobacco Products) and the reasons to restrain taxation on cigarette products. As a former Ohio Budget Director, I have an appreciation of the challenges facing your committee.

SB 233 is a statewide cigarette excise tax of \$1.50 or a 190% per pack increase affecting Kansas retailers, wholesalers and potentially over 400,000 Kansas adult smokers.

A cigarette tax increase, in particular a large rate increase, is likely to hurt Kansas small businesses, including mom-and-pop retail stores that rely on cigarette sales. A loss of cigarette sales is accompanied by a loss of sundry sales, or secondary purchases estimated at twenty cents for every dollar of cigarette sales. The loss of cigarette and sundry sales results in a loss of profits and state sales taxes. Kansas business groups can more properly provide examples of the negative economic impact of a cigarette tax increase, including the potential loss of Kansas jobs.

The cigarette excise tax is an unreliable, declining revenue source. Smoking bans, health concerns and other factors have resulted in a national pack drop averaging two percent or more per year. Since Fiscal Year 2004, Kansas legal pack sales have declined more than 25 percent without a tax rate increase. The Fiscal Year 2003 tax rate increases totaled 229 percent and produced a 146 percent increase in Fiscal Year 2004 excise tax revenues which, as expected, has declined.

I question the assertion that a cigarette tax increase will result in a material reduction in cigarette use. Actually, the tax increase may provide a further incentive for Kansas smokers to utilize alternative markets, some of which are likely tax-free.

An unintended consequence of higher tobacco tax rates is smuggling. The Mackinac Center for Public Policy recently predicted increased smuggling if the Kansas cigarette tax is enacted and predicts substantial drops in legitimate tax sales.

Additional cross-border sales are likely as the proposed 190 percent increase to the cigarette tax rate would place Kansas higher than all border states. The current Kansas cigarette tax is 4.6 times the Missouri rate and would expand to 13 times the Missouri rate. And, of course, over 40 percent of Kansas's population reside in the Kansas border counties.

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Cigarettes are abundant on the Internet, resulting in lost state sales taxes and lost state excise taxes. And the newest option for smokers is vapor products. Smokers are switching to vapor products, a market growing at a rapid rate. One source estimates 1.0-1.5% of smokers¹ (420,000-630,000 nationally) switch to e-vapor products each year.

If the \$1.50 per pack increase is enacted, it is estimated that Kansas will experience a net gain in cigarette excise tax revenues, even with a pack loss caused by the rate increase. But, again, Kansas will also realize a loss of cigarette sales and sundry sales, a profit loss and a sales tax loss from the proposed cigarette tax increase. Note that the sales tax loss applies to the state and to over 800 city/county jurisdictions.

Lastly, a cigarette tax is a regressive tax affecting a small number of Kansas adults. It is a tax on the poor paid by those least able to pay. Higher retail cigarette prices resulting from rate increases do not restrict the rich from purchasing but are likely to affect low income consumers.

Other tobacco products (OTP), while not experiencing the annual cigarette volume drop, are similar to cigarette taxation in that Kansas businesses will be affected, cross-border and Internet sales may increase, and the OTP excise tax is regressive.

The rejection of a cigarette tax increase is a recognition that:

- Kansas businesses will experience lost sales, lost profits, and possibly lost jobs
- Cigarette taxes are an unreliable and declining tax revenue source
- Smokers have options in response to excise tax rate increases
- The cigarette tax is regressive and hurts the most vulnerable
- Cross-border, Internet and smuggling options are likely to increase, and
- Kansas will lose state, city and county sales tax revenue

I urge you to reject the proposed cigarette and Other Tobacco Product excise tax increases.

Thank you for the opportunity to present information to the committee. I will attempt to answer any questions you may have.

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¹ Wells-Fargo Securities, Bonnie Herzog, Managing Director, Beverage, Tobacco & Convenience Stores Research