



INTERNET SALES OF TOBACCO PRODUCTS – REACHING KIDS & EVADING TAXES –

The ongoing increase in illegal Internet sales of tobacco products is stealing away billions of dollars in federal and state tobacco tax revenues and presenting a major challenge to public health efforts to reduce smoking, especially among youth. By failing to do adequate age verification, the rapidly growing number of websites selling tobacco products make it easier and cheaper for kids to buy cigarettes. Internet tobacco product sales also offer smokers an easy way to evade paying applicable federal, state, and local taxes, thereby reducing government revenues, keeping cigarette prices down, and keeping smoking levels up.¹ There is also a concern that Internet cigarette trafficking provides a funding source for terrorist organizations.²

Internet Cigarette Sales Are Growing – Fast. In 2006, there were more than 770 websites selling cigarettes to U.S. smokers, with about half based outside the USA – up from approximately 40 domestic Internet sellers of cigarettes in early 2000.³ No recent nationwide data on Internet purchases is available, but past surveys showed the portion of adult smokers buying cigarettes online rising from 0.6 percent in 2002 to 1.3 percent in 2002 (amounting to well over half a million smokers).⁴ But the online buying rates were much higher in several state studies. For example, a New Jersey study found that the number of smokers who had ever purchased from the Internet had grown from 1.1 percent in 2000 to 6.7 percent in 2002, with similar increases in the number regularly buying over the Internet.⁵

Since then, the problem has increased enormously. Most directly, since 2002 the number of people in the United States with Internet access increased by more than 60 percent and consumer purchases over the Internet have increased by more than 50 percent.⁶ Not surprisingly, a 2004 survey in New York found that ten percent of adult smokers often buy their cigarettes online with another five percent having done so in the past year.⁷ Similarly, a 2004 New Jersey study found that ten percent of smokers usually purchased their cigarettes from the Internet with 19 percent having purchased online at some point in the past.⁸ As cigarettes become even more expensive, both from cigarette company price hikes and increases to tobacco tax rates, this upward trend in Internet sales is likely to continue.

It is impossible to know exactly how many cigarettes are sold illegally over the Internet each year; but there are a number estimates. According to a Prudential Securities report, in 2002 Internet vendors sold roughly two percent of all cigarettes consumed in the United States, or more than 400 million packs per year, with Internet cigarette sales likely to triple within the next three years.⁹ A 2001 study by Forrester Research, Inc. projected that Internet cigarette sales would grow even more rapidly and account for 14% of the total U.S. market by 2005, or roughly \$5 billion in sales.¹⁰ Monitoring just a portion of all tobacco-selling websites, comScore Networks Inc. found that in a single month, November 2004, 1.1 million consumers visited more than 100 Internet cigarette retail sites.¹¹ How many cartons cigarettes those and all other U.S. Internet buyers purchased that day or that year is not known; but it is clear that the number is large.

Tax Evasion Through Internet Sales. Internet cigarette prices are much lower than cigarette prices in regular bricks-and-mortar retail outlets because Internet prices almost never include the cigarette state excise taxes and sales taxes and frequently evade applicable federal and local taxes, too. These tax-free low prices make Internet cigarettes attractive to both adult and underage smokers, and help to boost overall smoking levels. In addition, the inability of states to collect the applicable state taxes that are legally owed on these cigarettes and other tobacco products sold over the Internet is reducing state revenues. The previously mentioned Forrester Research report estimated that because of tax-evading Internet cigarette sales the states lost as much as \$200 million in tobacco tax revenues in 2001 and may lose as much as \$1.4 billion in 2005.¹²

Internet sellers usually buy the cigarettes they sell in a low-tax state (e.g., NC or SC, which have state cigarette tax rates of only 5 and 7 cents per pack, respectively and have no tax stamps) or purchase them free from any state tax (e.g., by selling cigarettes obtained outside the United States free of any U.S. state or federal taxes, or obtained in the United States but still free of state tax because they are meant to be sold

¹ Despite Internet-based tax evasion, every state that has significantly increased its cigarette tax rate has enjoyed a substantial increase in state revenues. For more info, see <http://tobaccofreekids.org/research/factsheets/pdf/0098.pdf>.

only to members of Indian tribes on Indian lands). The Internet vendors then sell these cigarettes to smokers in higher-tax states, typically without collecting those states' taxes. According to a 2002 U.S. General Accounting Office report, information posted on more than three quarters of all Internet-selling website also explicitly indicate that they do not comply with the Federal Jenkins Act, which requires Internet sellers to register with each state and provide monthly reports of their sales into the state. The GAO report also found that state efforts to prompt compliance by Internet sellers have not been successful, even when some Internet sellers make the required reports.¹³ Offshore websites that sell U.S. brands manufactured overseas or manufactured in the U.S. and exported for intended foreign sale not only evade state taxes but also regularly violate federal laws requiring payment of applicable federal taxes on imported cigarettes.

Youth Access to Tobacco Products Sold on the Internet. Effective safeguards against kids being able to purchase cigarettes via the Internet are almost non-existent. While many Internet websites post notices that sales to persons under 18 are illegal or not allowed, very few do anything at all to make sure such sales do not happen.

- An *American Journal of Public Health* study reported that almost 20% of cigarette-selling websites do not say anything about sales to minors being prohibited. More than half require only that the buyer say they are of legal age (e.g., by clicking on a "I am Over Age 18" button), another 15% require only that the buyer type in their date of birth, and only 7% require any driver's license information.¹⁴
- While some Internet vendors claim that credit card use, by itself, adequately safeguard against underage purchases, many kids have access to credit cards and the credit card companies (which specifically market cards for kids) have firmly stated that credit cards are not appropriate for age verification. In any case, more than two-thirds of websites selling tobacco products also accept money orders or checks.¹⁵
- Attorneys general from at least 15 states have conducted Internet "stings" and found that children as young as 9 years old were able to purchase cigarettes easily. A sting operation in New York found that 24 of 26 web sites sold to minors.¹⁶
- In a study published in the *Tobacco Control* journal, kids sent in orders to Internet cigarette vendors, providing a money order for the purchase but no proof of age, and only 14% of the orders were rejected because of the lack of proof of age.¹⁷
- A *JAMA* study found that more than 96 percent of minors aged 15 to 16 were able to find an Internet cigarette vendor and place an order in less than 25 minutes, with most completing the order in seven minutes.¹⁸
- A 2006 study of 101 Internet websites selling into California found that none of them complied with that state's laws regarding age and ID verification to stop sales to kids.¹⁹

There are no recent surveys on how many teenagers and other youth are buying cigarettes and other tobacco products over the Internet. But an old study from 2000 found that approximately 1.4 percent of high school smokers purchased their last pack from the Internet, as did one percent of middle school smokers, at that time.²⁰ A year later, another study found that more than three percent of smokers 12 to 17 had recently purchased cigarettes online.²¹ These dated findings still indicate that, at a very minimum, well over 100,000 children in the U.S. were buying tobacco products on the Internet more than five years ago.

Since then, however, the number of households with Internet access has grown enormously, as has youth access to credit and debit cards and youth familiarity with making Internet purchases. Even more disturbing a 2005 Kaiser Family Foundation survey found not only that Internet access among youth has increased from 47 to 74 percent from 1999 to 2004 but that 96 percent of all seventh to twelfth graders have gone on line, 38 percent have purchased something on line, *and almost a third have pretended to be older to gain access to an age-restricted website.*²² While new nationwide data on total youth purchases of tobacco products online is not yet available, a study in New York found that Internet purchases just by ninth graders (14 and 15 year olds) increased from 1.6% in 2001 to 5.2% in 2004-2005 –and online purchases are even more frequent among older youth smokers.²³

Ongoing increases in youth purchases of tobacco products over the Internet are likely given the lack of effective obstacles to youth Internet purchases and the growing differences between low Internet prices and

regular retail prices for cigarettes. In those states and localities with effective enforcement efforts to stop illegal sales by bricks and mortar retailers, Internet sellers offer youth an easily accessible alternative means for purchasing cigarettes. Because Internet cigarette vendors often require a two-carton minimum purchase, many high school and middle school buyers of Internet cigarettes also end up serving as suppliers of low-cost Internet cigarettes to their friends and classmates.

Other Problems with Internet Tobacco Sales

- Fewer than a third of all cigarette-selling websites display the Surgeon General's health warnings.²⁴
- Besides failing to comply with the federal Jenkins Act and state laws requiring age verification prior to sale, Internet sellers also typically fail to comply with state laws requiring all retail sellers of tobacco products to obtain licenses prior to making any sales in the state and fail to comply with various other laws and regulations that must be followed by regular bricks-and-mortar retailers in the states.
- Because Internet vendors of tobacco products are usually located out of state – or even out of the country – it is very difficult for state officials to enforce the state laws that apply to Internet sellers. In addition, many Internet sellers of tobacco products are based on Indian Lands, and related tribal sovereignty protections make state enforcement lawsuits against such Tribal Internet sellers that violate state laws very difficult, if not impossible. Even without that problem, the vast, growing number of Internet tobacco sellers – and the ability of smokers to switch quickly from one Internet vendor to another -- makes any lawsuit-based enforcement strategy expensive, time consuming, and largely ineffective.²⁵
- The many difficulties faced by states that wish to enforce their laws that apply to Internet tobacco product sales is compounded by the federal government's failure, to date, to enforce the Jenkins Act against the many Internet sellers that not only fail to comply but flaunt their noncompliance.²⁶

Campaign for Tobacco-Free Kids, April 28, 2008/ Eric Lindblom

More Information

Campaign website's special report on Internet tobacco sales: <http://tobaccofreekids.org/reports/Internet>.

TFK factsheets on Internet sales, <http://tobaccofreekids.org/research/factsheets/index.php?CategoryID=23> (includes model state legislation for blocking illegal Internet sales).

List, with links, to other related materials, <http://tobaccofreekids.org/reports/internet/resources.php>.

¹ See Connolly, G, "Smokes and cyberspace: a public health disaster in the making," *Tobacco Control* 10:299 (Winter), December, 2001, <http://tc.bmjournals.com/cgi/content/full/10/4/299>; Cohen, J, et al., "Tobacco commerce on the Internet: a threat to comprehensive tobacco control," *Tobacco Control* 10: 364-367 (Winter), December, 2001, <http://tc.bmjournals.com/cgi/content/abstract/10/4/364>.

² See, e.g., U.S. General Accounting Office, *TERRORIST FINANCING: U.S. Agencies Should Systematically Assess Terrorists' Use of Alternative Financing Mechanisms*, GAO-04-163, November 2003.

³ Ribisl KM et al., "Sales and marketing of cigarettes on the Internet: Emerging threats to tobacco control and promising policy solutions," in *Reducing tobacco use: Strategies, barriers, and consequences*, Washington, D.C.: National Academy Press; 2007. See, also, Prudential Financial, *Buying Cigarettes Over the Internet*, Research Report, Consumer Staples/Tobacco, September 24, 2002; Bryant, JR, et al., "Online Sales: Profit Without Question," *Tobacco Control* 11: 226-27, September, 2002, <http://tc.bmjournals.com/cgi/content/abstract/11/3/226> [citing Noack D, "Utah recruits kids to buy smokes online. Proposed laws would plug loopholes," *Salt Lake City*, February 2000]. Ribisl, KM, et al., "Web sites selling cigarettes: how many are there in the USA and what are their sales practices?," *Tobacco Control* 10: 352-359 (Winter), December, 2001, <http://tc.bmjournals.com/cgi/content/abstract/10/4/352>.

⁴ Hyland, A., F. L. Laux, et al., "Cigarette purchase patterns in four countries and the relationship with cessation: findings from the International Tobacco Control (ITC) Four Country Survey." *Tobacco Control* 15 Suppl 3: iii59-64, 2006.

⁵ Hrywna, M., et al, "Prevalence and Correlates of Internet Cigarette Purchasing Among Adult Smokers In New Jersey," *Tobacco Control* 13:296-300, September 2004, <http://tc.bmjournals.com>.

⁶ Nielson/Net Ratings Enumeration Study, <http://www.nielson-netratings.com>. U.S. Census Bureau, quarterly releases of retail e-commerce data, <http://www.census.gov/mrts/www/mrts.html>.

⁷ Davis, K, et al., *Cigarette Purchasing Patterns Among New York Smokers: Implications for Health, Price, and Revenue*, New York State Department of Health, Tobacco Control Program, March 2006, <http://repositories.cdlib.org/tc/surveys/NY2006>.

⁸ Kim, A, et al., "Smokers' Beliefs and Attitudes About Purchasing Cigarettes on the Internet, Public Health Reports 121: 594-602, Sept-Oct, 2006.

⁹ Prudential Financial, *Buying Cigarettes Over the Internet*, September 24, 2002.

¹⁰ Rubin, R. et al., *Online Tobacco Sales Grow, States Lose*, Forrester Research, Inc., April 27, 2001, <http://www.forrester.com/ER/Research/Brief/Excerpt/0,1317,12253,00.html>

¹¹ Tsai, M., "Crackdown On Otamedia Could Help U.S. Cigarette E-tailers," *Wall Street Journal Online*, January 28, 2005.

¹² Rubin, R. et al., *Online Tobacco Sales Grow, States Lose*, Forrester Research, Inc., April 27, 2001.

¹³ U.S. General Accounting Office, *Internet Cigarette Sales: Giving ATF Investigative Authority May Improve Reporting and Enforcement*, GAO-02-743, August 9, 2002, <http://www.gao.gov/new.items/d02743.pdf>. The Jenkins Act, 15 USC 375 et seq., is available at <http://www4.law.cornell.edu/uscode/15/ch10A.html>.

¹⁴ Ribisl, K, et al., "Are the Sales Practices of Internet Cigarette Vendors Good Enough to Prevent Sales to Minors?," *American Journal of Public Health* 92(6): 940-41, June 2002, <http://www.ajph.org/content/vol92/issue6/index.shtml>.

¹⁵ Unger, JB, et al., "Are adolescents attempting to buy cigarettes on the Internet?," *Tobacco Control* 10: 360-63 (Winter), December, 2001, <http://tc.bmjournals.com/cgi/content/abstract/10/4/360> [citing Kim AE, et al., "Sales practices of Internet cigarette vendors: Are they adequate to prevent minors from buying cigarettes online?," Roundtable presented at the Annual Meeting and Convention of the American Public Health Association, Boston, Massachusetts, November 2000].

¹⁶ Unger, JB, et al., "Are adolescents attempting to buy cigarettes on the Internet?," *Tobacco Control* 10: 360-63 (Winter), December, 2001 [citing Sherer R, "States crack down on Web tobacco sales," *The Christian Science Monitor*, November 8, 2000 & ABC News, "Getting smokes online: Children buying cigarette with click of mouse," March 6, 2001, <http://www.abcnews.com>].

¹⁷ Rubin, R. et al., *Online Tobacco Sales Grow, States Lose*, Forrester Research, Inc., April 27, 2001. For a more recent study, see Ribisl, K., et al., "Internet Sales of Cigarettes to Minors," *JAMA* 290(10): 1356-59, September 10, 2003, <http://jama.ama-assn.org>.

¹⁸ Jensen JA, et al., "Availability of tobacco to youth via the Internet," *JAMA (Journal of the American Medical Association)* 291(15):1837, April 21, 2004.

¹⁹ Williams RS, et al., "Internet cigarette vendors' lack of compliance with a California state law designed to prevent tobacco sales to minors," *Archives of Pediatrics and Adolescent Medicine*. 160(988-989), 2006.

²⁰ U.S. Centers for Disease Control and Prevention (CDC), *Youth Tobacco Surveillance – United States, 2000*, CDC Surveillance Studies, *MMWR* 50(SS-4), November 2, 2001, Table 23, <http://www.cdc.gov/mmwr/PDF/ss/ss5004.pdf> [according to CDC, the seemingly related national YTS Internet data in Table 22 of the 2000 YTS is completely inaccurate and unusable because of survey and formatting problems].

²¹ Substance Abuse and Mental Health Services Administration, *National Household Survey on Drug Abuse, 2001*.

²² Kaiser Family Foundation, *Generation M: Media in the Lives of 8-18 Year-olds*, March 9, 2005, <http://www.kff.org/entmedia/entmedia030905pkg.cfm>.

²³ Fix, BV et al., "Internet Cigarette Purchasing Among 9th Grade Students in Western New York: 2000-2001 vs. 2004-2005," *Preventive Medicine* 43(3): 191-195, September, 2006.

²⁴ Ribisl, KM, et al., "Web sites selling cigarettes: how many are there in the USA and what are their sales practices?," *Tobacco Control* 10: 352-359, December, 2001, <http://tc.bmjournals.com/cgi/content/abstract/10/4/352>.

²⁵ See the Campaign factsheet, *The Critical Importance of a Delivery-List Enforcement Provision in State Internet Tobacco Sales Legislation*, <http://tobaccofreekids.org/research/factsheets/pdf/0259.pdf>, for an effective state enforcement alternative, s

²⁶ U.S. General Accounting Office, *Internet Cigarette Sales: Giving ATF Investigative Authority May Improve Reporting and Enforcement*, GAO-02-743, August 9, 2002, <http://www.gao.gov/new.items/d02743.pdf>.