



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

Ongoing 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. According to the most recent formal survey, there were more than 700 Internet websites selling cigarettes to U.S. consumers in 2006, up from only a handful in the late 1990s.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 late 2002 to 1.3 percent just seven months later (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 New Jersey study found that in 2004 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

^{*} 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>.

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 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

**More information on Internet tobacco sales is available at
http://www.tobaccofreekids.org/facts_issues/fact_sheets/policies/internet/.**

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, December, 2001.

² See, e.g., Blumenthal, L., "Back Tax Asked on Cigarettes: \$4 million -- State sending out letters seeking payment," *The News Tribune*, March 29, 2004; Fairbanks, P., "Smugglers' Haven? Law Enforcers Say the Buffalo Niagara Region is a Hotbed of Cigarette Smuggling – Now a Federal Task Force Aims to Crack Down on the Crime," *Buffalo News*, Oct. 14, 2002; U.S. General Accounting Office, Terrorist Financing: U.S. Agencies Should Systematically Assess Terrorists' Use of Alternative Financing Mechanisms, GAO-04-163, <http://www.gao.gov/new.items/d04501t.pdf>, November 2003.

³ Personal correspondence from Professor Kurt M. Ribisl, Gillings School of Public Health, University of North Carolina at Chapel Hill, January 8, 2010 [citing data from his 2006 survey of 762 Internet sellers serving U.S. consumers (2009 data currently being tabulated)].

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.

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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>.

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

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- 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>.
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