

— LEGISLATIVE —
TESTIMONY

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MICHAEL D. LAFAIVE

Cigarette Tax Evasion and Avoidance in the Treasure State

Montana House Taxation Committee

Members of the Committee:

Thank you for allowing me to testify today about Montana House Bill 826, which proposes to add a dollar to the excise tax on cigarettes, raising it to \$2.70 per pack.

My name is Michael LaFaive and I am an economist with the Mackinac Center for Public Policy, a Michigan-based research institute. My colleague, professor Todd Nesbit, and I have long done research into cross-border economic activity. We have decades of experience exploring the economic impacts that state policy has across state, county and even international borders. The primary focus of our cross-border research has been cigarette tax evasion and avoidance, or what we call “smuggling.”

In 2008 we built a statistical model to measure the degree to which cigarettes are smuggled across the country, including imports from Mexico and exports to Canada. We update that model every year. It tells us that Montana’s net smuggling rate is 21% through 2022. In other words, one in five cigarettes getting smoked in Montana does so without anyone having paid the state cigarette excise tax.

If Montana adopts HB 826 and its 59% excise tax increase, our model predicts that smuggling will increase by 12 percentage points, making smuggling one-third of the total market.

High excise taxes on cigarettes turn each pack of cigarettes into a little gold bar that organized crime elements can use to increase their own treasure at the expense of the Treasure State’s fisc. They also incentivize smokers to shop in lower-taxed jurisdictions.

None of this should suggest my colleague and I want people to smoke. We have never smoked cigarettes, we don’t want you to do so, and if you do, we’d like to see you kick the habit.

What we do want to do is make sure your policy decisions are informed by their expected consequences. Not only do cigarette tax hikes come with expensive unintended effects, but they often lack the promised gains to public health. In the face of higher taxation, people often smuggle rather than quit.

Cigarette taxes are already so high in many states that one 2014 study in the journal “Economic Inquiry” shows that it would take a 100% increase to reduce adult smoking rates by just 5%.

Thank you for your time and attention.

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