Organized Crime and Illicit Trade in Tobacco Products in California

A proposal for the 2018 International Criminology Conference

Authors
Jonathan Kulick (New York Univ.) and James Prieger (Pepperdine Univ.)

Presenter
Jonathan Kulick

Brief abstract
Illicit trade in tobacco products (ITTP), which is attractive to smokers seeking to avoid high tobacco taxes, involves both small- and large-scale organized criminal activity. ITTP is conducted by entities ranging from large, structured organized criminal groups to small, flexible bands of traffickers. We investigate how ITTP increased in California after a large tax increase. The prevalence of each suspicious outcome or illicit activity examined rose after the tax increase by anywhere from 11% to 331%. We examine how such behaviors correlate with demographic, economic, and attitudinal factors. Evidence regarding the type of criminal supply is discussed.

Description of the paper

Objectives
Our study measures cigarette tax evasion, avoidance, and illicit trade before and after a large state tobacco tax increase. We investigate which economic, demographic, and behavioral factors are most strongly associated with such behavior, and which forms of illicit supply emerged.

Background
Demand-side responses to excise tax increases can include tax avoidance and evasion. Supply-side responses can include provision of untaxed or counterfeit (illicit) goods. In the case of tobacco taxes, such unexpected market responses can reduce the efficacy of increasing cigarette taxes toward reducing smoking and raising tax revenue.

Data/Methods
To investigate these issues, we commissioned surveys of California smokers before and after a large state tobacco tax increase in April 2017. We gathered information from respondents on their smoking habits and intended and actual responses to the tax increase. Particular responses we investigate
include quitting or reducing smoking, purchasing cigarettes online, out of state, or from Native American reservations, and seeking out other licit and illicit ways to reduce expenditure on cigarettes. We also estimate the prevalence of counterfeit product in the market. For sensitive questions about tax evasion and avoidance we employ the item count technique, a method shown to improve the accuracy of self-reported behavior.

Methods include estimation of population means and proportions, hypothesis testing of changes in those, and logit regressions of tax evasion on demographics, economic factors such as cigarette prices, and behavioral factors.

Results
Before the tax, half of smokers intended to act in ways that undermine the public health rationale for raising tobacco taxes. We compare these intentions with the actual (stated) behavior of smokers after the tax increase. Significant proportions of the smoking population engage in some measures of avoidance and evasion already before the tax (e.g., buying out of state, buying from sellers who did not pay required taxes). The prevalence of each suspicious outcome or illicit activity examined rose markedly after the tax increase—by anywhere from 11% to 331%. While some methods of procuring illicit cigarettes involve organized criminal supply, tax avoidance by cross a state line is more common. Some 63% of those still smoking in 2018 acted in ways that undermine, at least partially, the public health rationale for raising tobacco taxes.

About 44% of smokers engaged in some legal tax-avoiding behavior in the previous year, 15% evaded taxes through cross-border purchases, and 27% bought untaxed cigarettes in the state in the past month. (These behaviors overlapped substantially.) There is a much lower incidence of counterfeit product and sales of single cigarettes.

We test several hypotheses from the tax evasion literature after the logit estimations. We find evidence that factors pertaining to behavioral considerations (social norms, guilt and shame, and perceptions of fairness) are associated with illegal behavior in some estimations.

Implications of the study
The intended tax-avoiding and –evading behavior by some consumers implies that the impact of the tax on smoking cannot be accurately determined by data from tax receipts in licit markets. Once our post-tax surveying is complete, our study will give a more complete picture of actual market responses to the tax increase and discuss implications for policy toward smoking and public health. The study also highlights an area of (typically non-violent) economic crime that many smokers are comfortable with. Illicit trade in cigarettes also provides interesting comparisons with other illicit markets, including similarly non-violent ones (e.g., counterfeit luxury products) and much more violent ones (e.g., illicit cocaine and heroin markets).