

Amend Revenue and Taxation Code (RTC) Section 30473.5 of the Cigarette and Tobacco Products Tax Law to specify that any person who possesses, sells, or offers to sell, or buys or offers to buy, any used cigarette tax stamps is guilty of a misdemeanor and subject to applicable criminal penalties. Also authorizes the Board of Equalization (BOE) to seize and destroy used cigarette tax stamps aggregated for reuse purposes.

Source: Investigations Division

Existing Law. Existing law¹ imposes an 87-cent excise tax on each pack of cigarettes (generally 20 cigarettes in each pack). The law requires cigarette distributors to pay the tax by purchasing cigarette tax stamps. Distributors are required to attach the stamp to each pack of cigarettes prior to distribution.

Under existing law,² any person who possesses, sells, or offers to sell, or buys or offers to buy, any false or fraudulent cigarette tax stamps is guilty of a misdemeanor, punishable by a fine or imprisonment up to one year in a county jail, or by both the fine and imprisonment.

To ensure compliance with the law, existing law³ authorizes a BOE employee to inspect any place for which there is evidence of a taxpayer's failure to comply. The law⁴ subjects any cigarette product to seizure and forfeiture when the stamp is affixed or the tax is paid in a manner that violates the law, whether or not the violation is subject to a defense, as provided. As a nonsalable product, the law authorizes the BOE to destroy the forfeited cigarettes.

Existing law does not provide for the seizure and destruction of used cigarette tax *stamps* aggregated for reuse purposes. Also, existing law has no criminal sanctions or penalties related to a person's possession, sale, or purchase of used cigarette tax stamps.

Current issues. Cigarette tax stamps, resembling stickers, are encrypted with the date, distributor's information, and the cigarette brand. The BOE's inspection teams authenticate tax stamps through the use of specified scanning devices which, among other things, show that the scanned stamps belong to that specific cigarette brand.

The BOE inspection teams have recently identified cigarette tax evasion schemes involving reused cigarette tax stamps. For example, an inspector's scan revealed that a stamp affixed to a Marlboro-branded pack had originally been applied to a Camel-branded pack. In these situations, while the distributor appropriately paid the cigarette tax through his or her stamp purchase and appropriately affixed the stamp to the product, the stamp itself was subsequently reused and affixed to another cigarette pack.

These used stamps can be acquired simply from (1) a trash bin search, where a consumer discarded his or her empty cigarette pack, (2) by retailers, who may offer to unwrap the pack for a customer during a sale and, in doing so, retain the wrapper containing the stamp, or (3) by other means.

By applying used stamps to an untaxed cigarette pack, taxpayers may evade the tax and disguise duty free, counterfeit, stolen, smuggled, and otherwise untaxed cigarettes as legitimate. The majority of these used stamps appear to be affixed to counterfeit and duty free cigarettes.

During inspections and joint operations with other law enforcement agents, staff has found retail shops accumulating a significant number of used stamps and storing them in places such as trash bags located

¹ Part 13 (commencing with Section 30001) of Division 2 of the RTC.

² RTC Section 30473.5.

³ RTC Section 30435.

⁴ RTC Section 30436.

behind the storefront counter or drawers behind the register area.

In a more sophisticated scheme discovered during an enforcement operation, staff found a storage unit containing 205,694 unaffixed used stamps with a tax value of \$178,954 placed on transfer sheets and prepared for affixation to cigarette packs. In this instance, the used stamps were also labeled by the cigarette brand to which they had been affixed originally. As a result, the unsuspecting consumer would receive a counterfeit pack of cigarettes and the tax would be evaded. Within the past year, staff also found an additional, larger collection of used stamps in a separate scheme, as well as numerous smaller collections at retail stores.

Cigarette tax stamps are generally not used for collectibles, as are postage stamps or trading cards. Therefore, used cigarette tax stamps do not have a value to the person collecting or aggregating them, except for tax evasion purposes.

This Proposal. This proposal makes it a misdemeanor for any person to possess, sell, or offer to sell, or buy or offer to buy, any used cigarette tax stamps. The crime is punishable by a fine of up to \$5,000 for less than 2,000 stamps, or up to \$50,000 for more than 2,000 stamps, or fine and imprisonment for not less than 1 year. This proposal also authorizes the BOE to seize and destroy used cigarette tax stamps aggregated for reuse purposes.

This proposal would allow the BOE staff and other law enforcement agents to combat this used tax stamp scheme by seizing and destroying them, minimize tax evasion opportunities, and assist in making the marketplace fair and equitable for those that are legitimately paying the excise tax.

Revenue Impact. The magnitude of the used stamp issue is unknown. However, assuming the tax value associated with the cases identified during the past 12 months is representative of future years, this proposal could deter tax evasion of about \$400,000 annually.

Section 30473.5 of the Revenue and Taxation Code is amended to read

30473.5. (a) Any person who possesses, sells, or offers to sell, or buys or offers to buy, any false, ~~or fraudulent, or unaffixed~~ stamps or meter impressions provided for or authorized under this part in a quantity of less than 2,000 is guilty of a misdemeanor, punishable by a fine not to exceed five thousand dollars (\$5,000) or imprisonment not exceeding one year in a county jail, or by both the fine and imprisonment.

(b) Any person who possesses, sells, or offers to sell, or buys or offers to buy any false, ~~or fraudulent, or unaffixed~~ stamps or meter impressions provided for or authorized under this part in a quantity of 2,000 or greater, is guilty of a misdemeanor, punishable by a fine not to exceed fifty thousand dollars (\$50,000) or imprisonment not exceeding one year in a county jail, or by both the fine and imprisonment. The court shall order any fines assessed be deposited in the Cigarette and Tobacco Products Compliance Fund.

(c) For purposes of this section, "unaffixed stamps" do not include any unused and unapplied rolls of stamps or loose stamps in possession of a licensed distributor.

(d) The board shall destroy any stamps seized under this section.