

# Legislative Analysis

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## COUNTERFEIT CIGARETTE PAPER & GRAY MARKET PRODUCTS: PROVIDE PENALTIES

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**House Bill 5052 as enrolled**  
**Public Act 238 of 2005**  
**Sponsor: Rep. Jacob Hoogendyk, Jr.**  
**House Committee: Judiciary**  
**Senate Committee: Judiciary**

### Second Analysis (8-16-06)

**BRIEF SUMMARY:** The bill would apply the current prohibitions and penalties that pertain to counterfeit cigarettes to counterfeit cigarette paper and to cigarettes and cigarette paper made in the U.S. for sale in other countries.

**FISCAL IMPACT:** The fiscal impact of this bill would depend on the penalties collected for the counterfeit cigarette paper, gray market cigarettes, and the gray market cigarette paper.

### **THE APPARENT PROBLEM:**

According to an ATF deputy director quoted in a Department of Justice press release dated August 22, 2005, "those who traffic in illegal weapons and counterfeit and contraband cigarettes pose a danger to our communities and our nation." Just as revenue from drug and weapons sales are used to fund criminal and terrorist activities, so is revenue from counterfeit cigarettes and gray market cigarettes. Gray market cigarettes and papers are products manufactured within the U.S. but intended for sale outside of the country. Independent brokers purchase the gray cigarettes or papers from foreign markets and re-import them into the U.S. They then are able to sell them at reduced prices because the products are exempt from state and federal taxes.

The trafficking of counterfeit cigarettes, papers, etc. is now a multi-billion dollar international industry with profits being diverted to various criminal and terrorist organizations. In July of 2002, the U.S. Immigration and Customs Enforcement (ICE) reported that agency investigations into tobacco smuggling increased by approximately 300 percent over three years. Others estimate that counterfeit sales now account for roughly 10 to 15 percent of the market.

Though the federal government largely enforces illegal tobacco sales, recent undercover sting operations reveal the important role that state and local agencies play when partnering with federal agencies. In an effort to assist the U.S. government in efforts to shut down illegal tobacco operations, and to protect state citizens and state revenue sources, legislation has been introduced to make it against the law to possess, sell, or transport counterfeit cigarette papers and gray market cigarettes and gray market cigarette papers.

## ***THE CONTENT OF THE BILL:***

Under the Tobacco Products Tax Act, it is a felony offense to possess, acquire, transport, or offer for sale contrary to the act 3,000 or more cigarettes, tobacco products other than cigarettes with an aggregate wholesale price of \$250 or more, or 3,000 or more counterfeit cigarettes. It is a misdemeanor offense if the number of cigarettes or counterfeit cigarettes involved is at least 1,200 but not more than 2,999 or if the tobacco products other than cigarettes have an aggregate wholesale value of \$100 or more but less than \$250.

House Bill 5052 would amend the act to also apply the above prohibitions to counterfeit cigarette paper, gray market cigarettes, or gray market cigarette paper. Similarly, the bill would apply a prohibition on falsifying a manufacturer's label on cigarettes or counterfeit cigarettes to gray market cigarette papers or counterfeit cigarettes. The penalty would remain the same as now – a felony punishable by imprisonment for not less than one year or more than ten years and the possible addition of a fine of not more than \$50,000.

"Counterfeit cigarette paper" would be defined as a cigarette paper with a false manufacturing label or that had not been printed, manufactured, or made by authority of the trademark owner. "Gray market cigarette" and "gray market cigarette paper" would mean any cigarette or cigarette paper the package of which bore any statement, label, stamp, sticker, or notice indicating that the manufacturer did not intend the cigarettes or cigarette papers to be sold, distributed, or used in the United States. This would include, but not be limited to, a label stating the cigarettes or cigarette papers were "For Export Only," "U.S. Tax Exempt," "For Use Outside U.S.," or, for gray market cigarette papers, "For Use In \_\_\_\_\_ (another country) Only," or similar wording.

The bill would also specify that the Michigan Department of Treasury would not have the authority to enforce the provisions of Section 8 regarding gray market cigarette papers or counterfeit cigarette papers. Currently, the attorney general and prosecuting attorneys of the state have the authority to enforce the Tobacco Products Tax Act and the department or its duly authorized agent can request the state police and all local police authorities to enforce the provisions of the act. These provisions would remain unchanged.

The bill would not change the penalties currently in the act: a felony offense is punishable by a fine of not more than \$50,000 or imprisonment for not more than five years, or both, and the misdemeanor offense is punishable by a fine of not more than \$5,000 or imprisonment of not more than one year, or both.

MCL 205.422 and 205.428

## ***ARGUMENTS:***

### ***For:***

In 2004, legislation was enacted that provided penalties for selling, possessing, and transporting counterfeit cigarettes. The illegal trafficking of tobacco products has grown

to be a huge money maker for criminal and terrorist organizations and so presents a very real danger to individual safety and to homeland security. In addition, illegal cigarette trafficking hurts Michigan residents by robbing the state of millions of dollars of tax revenue needed to fund necessary state programs and services. Businesses, including manufacturers and mom and pop retailers, are also hit hard by economic losses due to counterfeiters. In July of 2005, a Michigan resident was sentenced in U.S. District Court (Western District) in Louisiana for trafficking in counterfeit ZigZag cigarette papers. As part of his sentence, he was ordered to pay ZigZag over half a million dollars in restitution. Many more millions in lost revenue to the state and businesses are never recovered. Therefore, it is now apparent that it is necessary to also outlaw the sale, possession, and transport of counterfeit cigarette papers and gray market products.

***For:***

From an administrative standpoint, the bill could have been problematic for the Department of Treasury to enforce, but a Senate floor amendment alleviating the department from having to enforce the provisions regarding gray market cigarette papers and counterfeit cigarette papers resolved the issue. Since the state does tax cigarettes, it isn't a problem to enforce the prohibition on selling cigarettes without a tax stamp or selling counterfeit cigarettes as it is easy to tell the legal from the illegal ones. However, since cigarette papers and gray market cigarettes and gray market cigarette papers are not taxed by the state, it could have been more difficult to tell which ones were illegal. In addition, it could have taken up to four additional full-time employees (FTEs) to adequately authenticate the packaging and enforce the prohibition, and, in light of the state's ongoing budget situation, there is no money for additional staff.

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