



OHIO WHOLESALE MARKETERS ASSOCIATION

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Testimony on the State Budget (HB49)

Beth Wymer, Executive Director

Senate Finance Committee

May 31, 2017

Chairman Oelslager and members of the Senate Finance Committee, thank you for the opportunity to provide my membership's perspectives on tax increases and the state budget. As you know, HB 49 as introduced included significant tobacco category tax increases, taxed e-cigarettes and vapor, reduced the wholesaler cigarette stamping compensation and eliminated the compensation wholesalers receive for collecting and remitting other tobacco product taxes. The House did remove the tax increases and reinstated the wholesaler compensation which OWMA supports and appreciates.

The Ohio Wholesale Marketers Association's core membership is wholesalers who supply products to convenience stores (c-stores), mom-n-pop corner stores and similar retailers. With few exceptions, the Association's distributor members are Ohio-based family-owned businesses that have served their communities for one or more generations. Wholesalers to c-stores are high volume low profit margin businesses, with the typical wholesaler having a pretax profit margin of about one percent.

These wholesalers sell much more than just tobacco, but the tobacco category-- which includes cigarettes and all other tobacco products--accounts for 70 to 80 percent of a typical wholesaler overall sales volume. For the smallest wholesalers, the category can be up to 90 percent of overall sales.

Cigarette and tobacco product taxes are not collected in stores at the register. These taxes are collected and remitted at the wholesale level so consequently, tax increases have an immediate and direct impact on these wholesale businesses.

Business Impacts for Wholesalers

Wholesaler Costs for Cigarette Tax Stamps: OWMA's wholesalers are the state's tax agents and frontend payers of the cigarette tax. The tax is an immediate tax on wholesalers who must buy cigarette excise tax stamps from the state and apply the stamps to each pack of cigarettes before selling the product to retailers. The stamp is proof that the tax has been paid.

At today's tax rate of \$1.60/pack, 12 rolls of tax stamps – the amount needed by a typical small wholesaler per month – costs the wholesaler \$565,000. A typical mid-size wholesaler runs through about 40 rolls of tax stamps/month at a cost of more than \$1.88 million.

Risk of loss from unpaid accounts/account receivables: There is no law requiring that wholesalers be paid on delivery for cigarettes or other tobacco products (there is such a law for beer/wine) so based on payment terms with retailers, it's about 14 to 20 days from the time the manufacturer debits the wholesalers bank account for the cost of the products until the wholesaler is paid by the retailer; during this time, the wholesaler carries the entire cost of the product and the excise tax. Increasing the tax increases the risk of nonpayment associated with the wholesaler's account receivables. Wholesalers are still obligated to remit the taxes to the state, even if the retailer doesn't pay for the taxed product.

Insurance on the State's Tax, ie on stamps in inventory. Higher tax rates mean higher costs to insure stamp rolls in the warehouse. Increasing the tax increases the value of the tax stamped cigarettes in the warehouse and when they are out on delivery trucks to retailers.

Insurance on the State's Tax, ie on stamps in transit. Two years ago, the Tax Department notified wholesalers that if tax stamps were lost in transit from the state to the wholesaler, the wholesaler is responsible for the full value of the stamps. Higher tax rates mean higher costs to insure the stamps in transit.

Loss from Theft Please see Attachment examples.

Cigarette Stamping Compensation

Last fiscal year wholesalers remitted \$944 million in cigarette taxes to the state. These are not the wholesalers' taxes --- these are the state's taxes and the wholesalers are doing a service for the state at significant cost to their businesses.

When wholesalers buy the tax stamps from the state, their cost per roll is the full value of the roll minus 1.8% which is compensation to the wholesalers for their costs associated with being the state's cigarette tax payer. Wholesaler costs include FedEx/UPS shipping charges to get the stamps from the state; insurance on stamps as outlined previously; cigarette stamping machine costs including maintenance and insurance on the machines, supplies needed for the machine and electric to run the machine; personnel; and monthly cigarette tax return filings with the state to report stamps bought and stamps used. Wholesalers are not making money on the stamping compensation, but it does rightfully help cover their costs.

Other Tobacco Products

Other tobacco products (OTP) are everything containing tobacco except cigarettes and the tax is calculated on the manufacturer price to the wholesaler. The wholesaler remits the tax each month based on shipments they received from manufacturers the prior month. As with cigarettes, wholesalers are the frontend tax payer and tax agents for the other tobacco products tax and if the retailer doesn't pay for the tobacco products the wholesaler is still obligated to remit the tax to the state.

One of the biggest challenges and frustrations when it comes to OTP is the reality of untaxed OTP getting into Ohio from lower taxed states. OTP traffickers sell to retailers who know they are buying untaxed product. They also buy some of the same product from a taxpaying wholesaler, just so they'll have an invoice available if enforcement agents stop by, and they mix the untaxed product in with the taxed product. It's very easy, very profitable and very hard to detect.

Any increase in the OTP tax rate increases wholesaler risk of loss from unpaid accounts/account receivables, increases insurance costs on inventory and does nothing more than give the already illegal operators who sell untaxed product more incentive to come into Ohio. This puts Ohio's taxpaying wholesalers at more of a disadvantage all while costing the state tax revenue that should otherwise be collected.

Last fiscal year wholesalers remitted more than \$63 million in other tobacco product taxes to the state. Just like with cigarettes, these are not the wholesalers' taxes --- these are the state's taxes and the wholesalers are doing a service for the state at a cost to their businesses. As the frontend tax payers and tax agents for the other tobacco products tax, wholesalers incur costs that include insurance on the tax as part of the product in inventory, cost associated with unpaid accounts/account receivables and costs associated with monthly tax report filings. Wholesalers are currently preparing their computer systems to compile and file their monthly OTP returns electronically, and that is also an added and ongoing cost.

New Vapor Tax

House Bill 49 as introduced included a new tax on e-cigarettes/vapor, taxing the products like other tobacco products. In addition to the stated concerns regarding OTP taxes, we expect that any new tax on the e-cigarette/vapor category will drive sales online meaning Ohio will not receive the expected tax revenue.

Border and Online Consequences to Consider

Cross Border and Online: Cross border and online sales do happen. When Ohio's cigarette tax increased by 70-cents/pack in 2005 - which was following a smaller increase a couple years prior - border counties in Ohio saw a **decrease** in pack sales ranging from 17.9% along the Indiana border to just short of 37% along the West Virginia border. At the same time, sales in Indiana counties that border Ohio **increased** by 14% and in West Virginia by 24%. Ohio sales along the Kentucky border dropped by 18.5%, but sales just over the border in Kentucky increased by 26%.

Demonstrating the cross border impact even further is the more recent Pennsylvania cigarette tax increase, effective August 2016, which is driving business to Ohio stores. A quick check on wholesale to retail shipment data for just three Ohio stores near Pennsylvania show that shipments increased for each store following Pennsylvania’s tax increase, and the higher sales volume has continued into 2017 for those Ohio stores.

Cross Border into Ohio Following Pennsylvania Cigarette Tax Increase (eff. 8/1/16)
Examples of Wholesale to Retail product shipments

Store Location	2015 Cigarette Cartons	2016 Cigarette Cartons	Total 2016 Cartons Before PA Tax Increase (Jan-July)	Total 2016 Cartons After PA Tax Increase (Aug - Dec)	2016 Jan – Feb Cartons	2017 Jan – Feb Cartons
Conneaut, OH	8811	9389	4681	4708	1089	1367
Lowellville, OH	7674	9939	3760	6179	1009	2054
Masury, OH	7548	8445	3953	4492	1074	1799
Totals	24,033	27,773	12,394	15,379	3,172	5,220

Keep in mind that “cross border” is not limited to state borders. The internet has broken the border barrier and tax-free cigarettes are available from a range of overseas websites. Even with shipping costs, major brands through these sites can cost less than 50 percent of the cost from an Ohio store at today’s tax rate. Tax free cigars and all other segments of the other tobacco product category plus the entire e-cigarette vapor category are also available online and those tax-free resources become more attractive to consumers when taxes are increased.



<http://www.dutyfreedepot.com/buy-duty-free-cigarettes.htm>

<http://dfreeshop.com/faq/>

Search Term Examples: “tax free cigarettes” – “tax free tobacco” – “tobacco online” – “cigarettes online” – “ecigs and vapor online”

Mr. Chairman and members of the committee, thank you again for this opportunity to submit comments and as always, please do not hesitate to contact me if you have any questions.

TOBACCO RELATED CRIME AGAINST OHIO BUSINESS

Examples of crime against tobacco wholesalers, as reported in by members of the Ohio Wholesale Marketers Association

March 29, 2017

Beth Wymer
Executive Director
Ohio Wholesale Marketers Association
88 E. Broad Street, Suite 1240
Columbus OH 43215

Beth,

I am writing this letter to bring to your attention the serious problem [REDACTED] is facing as a wholesale distributor of cigarettes. We have had a significant increase in our truck drivers being robbed of product during store deliveries. We were robbed on 5/23/16, 5/26/16, 12/30/16, 1/30/17 and 3/17/17. The latest one was done at gunpoint with our driver being forced to lay face down in the back of the truck while the thieves hauled away over \$9,000 in product.

If this latest proposed tax increase of an additional \$6.50 per carton passes I am fearful that we will have to start delivering in armored vehicles. I know of other distribution companies who are considering paying for concealed carry classes for their drivers. I can't imagine how that will turn out.

I and other wholesalers are at wits end trying to come up with a viable solution to this problem while still be able to run a profitable and safe business.

I would appreciate you communicating this issue to the appropriate representatives at the state and let me know their input.

Sincerely,

[REDACTED]

In the Cleveland market we had been strong armed robbed so many times.

- *Criminals just jumping up in the back of the truck while the driver was in the back of the truck and demanding a case or 2 of cigarettes, of course our company policy is to comply.*
- *Criminals carrying a set of bolt cutters, snapping the lock and taking what they want while the driver was in the store.*
- *We had a store owner with a gun chasing down a would be thieves that jumped up in the back our truck with the driver and tried to grab cases of cigarettes.*
- *We had a driver in the back of the truck, when a would be thief with a gun jumped in the back of truck demanding the keys to the truck, then locked the driver in the back of the truck and started down the road, the driver used his 2-wheeler to break out a panel of the back door and flag down a car. The driver of the car called the police and thank God the thief was caught before the situation got any worse. (That driver of 12 years never returned to work.)*

We now have a armed security company, in Cleveland, that leads our truck stop to stop and escorts the driver while delivering cigarettes and tobacco, then guards the truck during the rest of the delivery. The cost to have security is + \$40,000 a year.

In the Dayton market we had a gun pulled on a driver, we now have 2 drivers in the truck in that area. Additional Cost of \$22,500 a year.

It's not only the big city that cigarettes are like gold, the smaller towns we have just as much trouble.

Security for the warehouse has been up graded twice over the last 5 years at a cost of over \$50,000.

... I do have many other stories but think this gets the point across.

[REDACTED]

TOBACCO RELATED CRIME AGAINST OHIO BUSINESS

Below is the list of cigarette thefts in Ohio. In order to protect our drivers, we currently use security company to accompany three of our routes in the Cleveland area, to insure our driver's safety and protect company assets.

<i>Date</i>	<i>City</i>	<i>Carton Loss</i>
<i>11-10-2009</i>	<i>Cleveland</i>	<i>60</i>
<i>1-28-2010</i>	<i>Cleveland</i>	<i>30</i>
<i>1-27-16</i>	<i>Euclid</i>	<i>39</i>
<i>5-18-2016</i>	<i>Cleveland</i>	<i>58</i>
<i>6-8-2016</i>	<i>Euclid</i>	<i>30</i>
<i>2-22-2017</i>	<i>Cleveland</i>	<i>30</i>

This has been an ongoing issue in Ohio as well as Michigan, primarily the Detroit area. We spend approximately \$450 per route per week to protect our drivers and product with a security person.

With the average cost of a carton being around \$59.00 per carton, that adds up quickly and with only make \$2.00 or less per carton, it takes a lot of additional sales to make up the loss. And of course, there are the intangible costs of any physical or psychological distress related to the driver.

As prices for cigarettes goes up, so does the criminal activity.

Thanks



12/13/16

During delivery on 12/13/16 our driver delivered product in Lima, Ohio at 6.30 am . Upon exiting the storage area the truck had been stolen. The truck was located approximately 1000 feet from the store in a alley. Upon review of the remaining contents 180 cartons of cigarettes were not on the truck. \$9,244.88 Total value of our loss. Police investigated and as of 3/21/17 no recovery has been made.

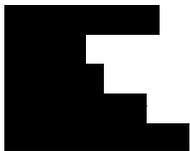
10/05/16

Delivery Truck rear door broken into while parked in our lot. Upon review 71 cartons of cigarettes were stolen and 17 rolls of snuff. 4,395.44 Total value of loss.

We invested over 5,000.00 to upgrade our security cameras after this incident.

It is important to note that the above incidents were the first theft cases we have been involved in.

Police were involved in both but no recovery or arrests have been made.



ITS ONLY GOING TO GET WORSE—I FORGOT TO MENTION WE INVESTED IN SPECIAL AUTO LOCK DOOR GIZMOS THAT WILL END UP COSTING AROUND 4000.00 WHEN COMPLETED



TOBACCO RELATED CRIME AGAINST OHIO BUSINESS

Here are pictures of our problems in 2016 with theft. We had 3 attempts, one being successful which caused way more damage than theft. Total theft of product was just a bit over \$5,000 but the damages cost us over \$15,000. Plus increasing security with new doors, fences, cameras brought our costs well over \$25,000 for the year. Some might argue that insurance will cover it and that damages to wholesalers are minimal but as you know insuring cigarettes is not easy or inexpensive. The fear is one or two claims and we could be without insurance or insurance that is way too expensive.

We've had a number of our customers who have had a vehicle driven through their building for less than 30 cartons of cigarettes. The damages can be 10 times what we have to pay for the stolen product.



I am the Director of Asset Protection for [REDACTED] ... During my time with the company (16yrs) I witnessed the correlation between significant price increases and the subsequent increase in acts of theft toward merchants who offer for sale or distribution cigarettes and tobacco products in general.

Although I could site many, two most recent incidents stand out during my time with [REDACTED] A few years ago, at two separate locations, and just a month apart, two of our [REDACTED] stores were burglarized resulting in major loses to the company. In each occasion, the perpetrator(s) displayed professional behavior relating to how security systems were disabled and how entry was gained.

In the first incident, the thief or thieves disabled sophisticated security systems, followed by cutting a hole in the store's roof to gain entry. Once inside and having disabled our security systems, they moved freely and undetected resulting in the removal of thousands of dollars in tobacco products, primarily cartons of cigarettes.

The second incident was eerily similar, once again, after disabling our security systems, the thief or thieves meticulously removed several concrete blocks from an outside store wall to gain entry. As had happened in the first example, with our systems disabled, they were able to move freely and undetected resulting in the removal of thousands of dollars in tobacco products, primarily cartons of cigarettes.

I am pleased to report, both cases were solved and in both cases the same individual was responsible. The subject in both burglaries admitted the thefts were a result of the increased cost of the products and the items obtained were being sold on the street to individuals at a significantly lower price.

I site these two cases as examples of how the security measures of tobacco merchants has increased to protect their products, but unfortunately, so too have the efforts of those seeking to obtain such a high demand and increasingly expensive product through whatever means possible.

I have been in the retail Loss Prevention field for more than 30yrs. I can clearly and without reservation state to you that the efforts to obtain tobacco products through theft and other nefarious means has increased significantly based on the continued increases imposed on tobacco products, and I fear this trend has no end in sight.

Respectfully,

[REDACTED]