



Office of the Speaker
BENJAMIN J.F. CRUZ
I Mina'trentai Kuåtro na Liheslaturan Guåhan
Committee on Appropriations and Adjudication

July 26, 2018

Mr. Shawn N. Anderson
Acting United States Attorney
U.S. Attorney's Office for the Districts of Guam and the NMI
Sirena Plaza, Suite 500
108 Hernan Cortez
Hagåtña, GU 96910

Mr. Sean Kaul
Special Agent in Charge
Federal Bureau of Investigation
91-1300 Enterprise Street
Kapolei, HI 96707(808) 566-4300

Re: Request for Investigation of Illicit Schemes to Underreport and Evade Cigarette Taxes in the Territory of Guam

Dear Mr. Anderson and Mr. Kaul:

As the Speaker of the 34th Guam Legislature, I am writing to notify the U.S. Attorney's Office and the Federal Bureau of Investigation of potential violations of federal and Guam law relating to the underreporting and non-payment of cigarette taxes by Mid Pac Distributors ("Mid Pac"), the distributor of Philip Morris branded cigarettes on Guam. The admitted failure of Mid Pac to report and pay over \$14.5 million in local cigarette taxes in the past three years requires federal agencies to investigate the possibility of tax evasion and diversion of cigarette activities—cigarette smuggling—in violation of federal and Guam law spanning beyond the reported three (3) year period.¹

As you are aware, Guam requires all imported cigarettes be placed in a bonded warehouse until such time the cigarette tax is paid before they can be sold by a wholesaler such as Mid Pac. One obvious way to avoid payment of cigarette taxes is to divert all or a portion of the shipment of cigarette to avoid reporting and payment of cigarette taxes.² Mid Pac *may* control approximately 50% of the cigarette market on Guam, and based on the Department of Revenue & Taxation monthly reports, assuming other cigarette distributors are paying their portion of the cigarette tax, there is a potential underreporting of as much as 30% of the total cigarette taxes due in the range of \$750,000 to \$1,000,000 per month, possibly attributable to Mid Pac alone.

¹ For example, the Prevent All Cigarette Trafficking Act of 2009 (the "PACT Act"), Pub. L. No. 111-154, amends the Jenkins Act (15 U.S.C. §§375-378) and the Contraband Cigarette Trafficking Act (18 U.S.C. §§ 2341-2346), "revising provisions that govern the collection of taxes on cigarettes and smokeless tobacco. Pub. L. No. 111-154 (2010). The amendments included a requirement for Internet and other delivery sellers to pay all applicable state and local excise taxes and affix any related tax stamps before delivering any cigarettes or smokeless tobacco products to any customer in a state." *See* Illicit Tobacco: Various Schemes Are Used to Evade Taxes and Fees, Report to Congressional Committees, GAO-11-313, at 5 (March 2011). The PACT Act defines "state" to include U.S. territories and possessions.

² *See id.* at 16 (listing "Underreporting tobacco product sales to state governments" and "Underreporting cigarette sales to MSA states" as examples of illicit trade schemes used to evade taxes and fees).

This strongly suggests that a significant amount of cigarette sales by Mid Pac are going unreported and corresponding cigarette taxes unpaid.

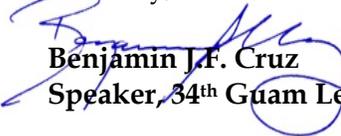
How the diversion of cigarettes is being accomplished needs to be investigated by the federal agencies charged with enforcement of federal laws. For example, "ATF enforces the Contraband Cigarette Trafficking Act (CCTA), which makes it unlawful for any person to ship, transport, receive, possess, sell, distribute, or purchase more than 60,000 cigarettes that bear no evidence of state cigarette tax payment in the state in which the cigarettes are found, if such state requires a stamp or other indicia to be placed on cigarette packages to demonstrate payment of taxes (18 U.S.C. 2342). . . . ATF inspections verify an applicant's qualification information, check the security of the premise, and ensure tax compliance."³ The 60,000 threshold was reduced to 10,000 in 2006 when Section 2342 of the CCTA was amended under Public Law 109-177.

In May 2018, the Public Auditor issued a report, as part of its Performance Audit of DRT's tobacco tax collections, stating that she lacked sufficient data to verify cigarette taxes to cigarette imports.⁴ The Public Auditor had requested information from Mid Pac, Philip Morris, and all other tobacco wholesalers and distributors relating to the amount of cigarettes imported by such companies and sold on Guam. Certain unnamed entities refused to provide any information requested by the Public Auditor. While I do not know if Philip Morris complied with the OPA's request, this company claims it is committed to "working with governments and other partners in the public and private sections to address [illicit cigarette trade]." *See* <https://www.pmi.com/glossary-section/glossary/illicit-cigarette-trade>. Now that Philip Morris is aware of public information regarding Mid Pac's failure to pay cigarette tax and possible diversion activities, it is imperative that Philip Morris cooperate in the investigation of Mid Pac's illicit schemes with respect to the importation, underreporting and non-payment of federal and local cigarette taxes.

It is important to ensure that federal and Guam's interests in promoting fair competition and preventing disruption of interstate commerce are protected. Furthermore, Guam is required to enforce local laws under the terms of the Master Settlement Agreement (the "MSA"), a settlement reached by participating tobacco manufactures and the States and Territories in 1998, which provides tobacco settlement payments to Guam. The MSA settlement payments secures the \$40 million GEDA Tobacco Settlement Revenue Bond. Guam is required under the MSA to diligently enforce its laws as it relates to reporting and the collection of cigarette taxes.

I hope that by bringing this to the attention of the federal authorities, you are able to assist Guam with enforcement by investigating and stopping further diversion, underreporting, and non-payment of cigarette taxes.

Sincerely,



Benjamin J.F. Cruz
Speaker, 34th Guam Legislature

³ See Internet Cigarette Sales: Limited Compliance and Enforcement of the Jenkins Act Result in Loss of State Tax Revenue, GAO-03-714T, at 5 (5/1/2003).

⁴

See Performance Audit of DRT Tobacco Tax, OPA Report No. 18-04 (May 2018), available at http://opaguam.org/sites/default/files/opa_report_no._18-04.pdf (last visited July 25, 2018).