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DEPT. COMM. NO. 534

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October 27, 2025

The Honorable Ronald D. Kouchi
President and Members of the Senate
Thirty-Third State Legislature
State Capitol, Room 409
Honolulu, Hawaii 96813

The Honorable Nadine K. Nakamura
Speaker and Members of the
House of Representatives
Thirty-Third State Legislature
State Capitol, Room 431
Honolulu, Hawaii 96813

Dear President Kouchi, Speaker Nakamura, and Members of the Legislature:

For your information and consideration, I am transmitting a copy of the Department of the Attorney General's Report on the Tobacco Enforcement Special Fund, as required by section 28-15(d), Hawaii Revised Statutes (HRS). In accordance with section 93-16, HRS, I am also informing you that the report may be viewed electronically at <https://ag.hawaii.gov/publications/reports/reports-to-the-legislature/>.

If you have any questions or concerns, please feel free to call me at (808) 586-1500.

Sincerely,

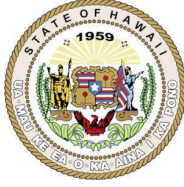
Anne E. Lopez

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c: Josh Green, M.D., Governor
Sylvia Luke, Lieutenant Governor
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Leslie H. Kondo, State Auditor
Luis Salaveria, Director of Finance, Department of Budget and Finance
Stacey A. Aldrich, State Librarian, Hawaii State Public Library System
Wendy F. Hensel, President, University of Hawaii

Enclosure

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REPORT ON THE TOBACCO ENFORCEMENT SPECIAL FUND

Pursuant to Section 28-15(d), Hawaii Revised Statutes

Fiscal Year 2024-2025

Submitted to the Thirty-Third State Legislature
Regular Session of 2026

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I. INTRODUCTION

Section 28-15(d), Hawaii Revised Statutes (HRS), requires the Department of the Attorney General (the Department) to submit a report to the Legislature, no later than twenty days prior to the convening of each regular session, providing an accounting of the receipts and expenditures of the Tobacco Enforcement Special Fund (the Special Fund).

On July 1, 2000, the Department's Tobacco Enforcement Unit (the Unit) was created to enforce the Tobacco Master Settlement Agreement, the state Tobacco Liability Act, chapter 675, HRS, the state Cigarette Tax and Tobacco Tax Law, chapter 245, HRS, and the state Tobacco Products Reporting Law, chapter 486P, HRS. The Unit is composed of a unit supervisor, a Master Settlement Agreement civil prosecutor, a cigarette tax prosecutor, six criminal investigators, a legal assistant, an auditor, and a legal clerk.

II. TOBACCO MASTER SETTLEMENT AGREEMENT

A. Background

On November 23, 1998, leading United States tobacco manufacturers entered into the Tobacco Master Settlement Agreement (Master Settlement Agreement or MSA) with forty-six states, including Hawaii. In consideration for a release of past, present, and certain future claims against them, the MSA obligates these manufacturers to pay substantial sums to the settling states (tied in part to the volume of tobacco product sales). The Attorney General of each settling state is responsible for enforcing the provisions of the MSA. The National Association of Attorneys General (NAAG) Center for Tobacco and Public Health ("NAAG Tobacco Center") was created as a result of the MSA, and provides legal counsel and representation to the attorneys general as they regulate the sale of tobacco and nicotine products in their states and enforce the MSA and related laws, regulations, and agreements. The Unit actively participates in NAAG Tobacco Center working groups, and that guides and directs the Unit's work of enforcing various provisions of the MSA. Members of the Unit currently participate in eighteen different NAAG working groups, working with NAAG and attorney general counterparts in nearly all the other states and territories in the United States. These working groups focus on a variety of topics, including internet stings; depictions of tobacco products, including cigarettes and e-cigarettes, across platforms such as the internet, social media, television, movies, and streaming; retail stores; e-cigarette directories; escrow release; legislation; new trending products; and many areas of enforcement required to diligently enforce the requirements of the MSA.

B. Master Settlement Agreement Payments

There are three types of MSA payments:

- (1) Initial Payments to Hawaii were received annually from January 10, 1999, through January 10, 2003.

Year	Amount of Initial Payment
1999-2000	\$ 27,804,177.13
2000-2001	11,659,558.77
2001-2002	12,701,627.03
2002-2003	12,864,378.74
Total	\$65,029,741.67

- (2) Annual Payments to Hawaii began on April 15, 2000, and are scheduled to be received on or about April 15 of each year in perpetuity.

Year	Amount of Annual Payment
1999-2000	\$ 20,811,042.90
2000-2001	24,471,822.21
2001-2002	32,674,220.28
2002-2003	31,845,690.90
2003-2004	37,793,157.48
2004-2005	38,357,998.54
2005-2006	35,212,822.31
2006-2007	36,857,166.01
2007-2008	37,299,996.79
2008-2009	41,132,845.88
2009-2010	34,230,792.73
2010-2011	32,453,603.85
2011-2012	33,096,749.95
2012-2013	33,073,205.78
2013-2014	37,420,086.29
2014-2015	32,022,781.47
2015-2016	33,654,568.07
2016-2017	33,211,083.41
2017-2018	26,149,213.01
2018-2019	34,801,958.14
2019-2020	35,309,044.26
2020-2021	37,461,342.15
2021-2022	38,442,830.77
2022-2023	40,862,842.25
2023-2024	36,427,417.26
2024-2025	33,809,139.01
Total	\$888,883,421.70

- (3) Strategic Contribution Payments to Hawaii began on April 15, 2008, and were received on April 15 of each year through 2017.

Year	Amount of Strategic Contribution Payment
2007-2008	\$ 18,762,802.27
2008-2009	19,225,534.21
2009-2010	16,691,299.06
2010-2011	15,211,574.73
2011-2012	15,492,087.49
2012-2013	15,505,806.17
2013-2014	15,238,278.95
2014-2015	15,206,293.27
2015-2016	15,612,254.40
2016-2017	15,538,756.05
Total	\$162,484,686.60

In fiscal year (FY) 2024-2025, the State received \$33,809,139.01 in MSA moneys. The total amounts of MSA payments received by Hawaii as of the end of FY 2024-2025 are as follows:

Initial Payments	\$ 65,029,741.67
Annual Payments	888,883,421.70
Strategic Contribution Payments	162,484,686.60
2004 Diligent Enforcement Arbitration Settlement of 2004 to 2017 Diligent Enforcement Arbitration issues*	58,600,584.78
Total	\$1,174,998,434.75

*Note: For more details on "2004 Diligent Enforcement Arbitration Settlement of 2004 to 2017 Diligent Enforcement Arbitration issues," refer to section II.F. (pages 8-9).

C. Tobacco Liability Act (Chapter 675, HRS)

The MSA requires the State to diligently enforce the requirements of the "model statute," which was enacted as the Tobacco Liability Act, chapter 675, HRS. The MSA and the Tobacco Liability Act represent affirmative steps toward holding tobacco manufacturers accountable for the harm caused by the sale of cigarettes to residents of Hawaii. Section 675-1(d), HRS, provides:

It is the policy of the State that financial burdens imposed on the State by cigarette smoking be borne by tobacco product manufacturers rather than by the State to the extent that such manufacturers either determine to enter into a settlement with the State or are found culpable by the courts.

Section 675-1(f), HRS, provides:

It would be contrary to the policy of the State if tobacco product manufacturers who decide not to enter such a settlement could use a resulting cost advantage to derive large, short-term profits It is thus in the interest of the State to require that such manufacturers establish a reserve fund to guarantee a source of compensation and to prevent such manufacturers from deriving large, short-term profits and then becoming judgment-proof before liability may arise.

The Tobacco Liability Act requires any tobacco product manufacturer selling cigarettes to consumers in Hawaii – whether directly or through a distributor, retailer, or similar intermediary or intermediaries – to either participate in and perform its financial obligations under the MSA, or place funds in an escrow account to establish a reserve fund to guarantee a source of compensation to the State if the tobacco product manufacturer is found culpable by the courts. (Section 675-3, HRS). A non-participating manufacturer (NPM) is a tobacco product manufacturer who has not entered into the MSA.

NPMs who fail to comply with the escrow requirements enjoy a price advantage over those who comply. This price advantage lures consumers away from and decreases the market share of participating manufacturers (PM).

In 2022, the Department proposed a bill to enable NPMs to assign their interests in any moneys in qualified escrow accounts to the State. A financial institution, acting as the escrow agent, would then be able to petition in court to transfer funds to the State when an escrow account is abandoned. The bill was signed into law on June 17, 2022 (Act 93, Session Laws of Hawaii 2022), and was codified as section 675-4, HRS. Section 675-4 facilitates the closure of abandoned escrow accounts in a timelier fashion, thus making continued administrative monitoring unnecessary. Section 675-4, HRS, also supports tobacco prevention and control as it allows the transfer of funds from the escrow accounts into the State's Tobacco Settlement Special Fund, under chapter 328L, HRS. This should prove useful in the coming years, as the first releases of escrow to NPMs began in 2025, after the money had been held in escrow for twenty-five years.

D. Enforcement

The biggest arbitration risk to states arising from the MSA involves the NPM Adjustment. Under the MSA, PMs can contest the diligent enforcement of states in hopes of reducing the money that they pay into the MSA. Failure to diligently enforce the Tobacco Liability Act may result in a state losing a significant portion of its MSA payments. "Diligent enforcement" in the context of the MSA enforcement had not been clearly defined and was the subject of the lengthy 2003 Diligent Enforcement (DE) Arbitration, which began in 2010 and concluded in 2013. In the 2003 DE Arbitration, the panel concluded that diligent enforcement was an ongoing and intentional consideration

of the requirements of a settling state's qualifying statute, and a significant attempt by a settling state to meet those requirements, considering a settling state's competing laws and policies that may conflict with its MSA contractual obligations. The factors considered by the 2003 panel included: collection rate, lawsuits filed, gathering reliable data, resources allocated to enforcement, preventing non-compliant NPMs from future sales, legislation enacted, actions short of legislation, and efforts to be aware of National Association of Attorneys General and other states' enforcement efforts.

On the issue of what constitutes "Units Sold," the 2003 arbitration panel determined that, "as a matter of law," the model statute definition of "Units Sold" is "unambiguous and binding." "Units Sold" is defined in Exhibit T to the MSA as follows:

"Units Sold" means the number of individual cigarettes sold in the State by the applicable tobacco product manufacturer (whether directly or through a distributor, retailer or similar intermediary or intermediaries) during the year in question, as measured by excise taxes collected by the State on packs (or "roll-your-own" tobacco containers) bearing the excise tax stamp of the State [Emphasis added.]

Simply put, the 2003 arbitration panel held that a state's obligation to collect escrow was limited to the NPM cigarettes that could be measured by packs bearing the excise tax stamp of a state.

Hawaii's diligent enforcement efforts and regulatory scheme include identifying NPMs and the number of NPM cigarettes sold in Hawaii in each calendar year; notifying NPMs of their obligation to establish and fund an escrow in accordance with chapter 675, HRS; and filing complaints in court against NPMs who fail to comply with chapter 675, HRS. The Department has developed a system that:

- (1) Identifies NPMs and their products;
- (2) Gathers and tracks information on NPM products;
- (3) Notifies NPMs of their obligations under the Tobacco Liability Act, Tobacco Products Reporting Law, and related statutes (the Department sends letters to tobacco product manufacturers worldwide to advise them of these obligations);
- (4) Provides assistance to effectuate compliance;
- (5) Supplies relevant information that allows the Department to file lawsuits as necessary to compel compliance with the escrow statutes; and
- (6) Provides the information-gathering and certification protocols necessary to establish and publish the directory of tobacco product manufacturers whose cigarettes and Roll-Your-Own (RYO) tobacco products are authorized for sale in Hawaii.

In 2003, the Unit created a directory of compliant cigarettes and RYO tobacco products. The directory has been posted on the Department's website since October

31, 2003, and has been revised and updated annually, up to and including through FY 2024-2025. At the end of FY 2024-2025, fourteen compliant tobacco product manufacturers (fourteen PMs and zero NPMs) were listed in the directory, along with a list of seventy-six authorized brands of cigarettes and RYO tobacco products.

Further, the directory, in conjunction with the Tobacco Products Reporting Law, chapter 486P, HRS, facilitates the time-consuming process of identifying individual manufacturers and their respective brands. When a tobacco product manufacturer is identified as having or intending to have sales in Hawaii, the Unit notifies the tobacco product manufacturer that it must comply with chapter 486P, HRS, including the requirement to register with the Department pursuant to section 486P-5, HRS.

The Unit provides a reporting form to wholesalers and distributors and gathers information from the wholesalers' and distributors' responses and invoices. Based on this information, the Unit verifies that only compliant NPMs and their brands are sold (directly or through distributors, retailers, or similar intermediaries) in Hawaii. In addition, by investigating cigarette brands on store shelves, the Unit verifies that only compliant NPMs and their authorized brands are stamped and sold in Hawaii.

On June 6, 2023, Governor Josh Green signed into law Act 62, Session Laws of Hawaii 2023. Starting July 1, 2023, wholesalers and dealers of electronic smoking devices (ESDs) and e-liquids were required to have a tobacco license with the Department of Taxation (DOTAX). Tobacco licensees have statutory obligations that arise under chapters 245 and 486P, HRS, which include monthly reporting requirements to the Unit. The Unit closely monitors these monthly reports, which detail the shipment of cigarette and tobacco products into Hawaii.

To prepare for the influx of these additional license reports, the Unit launched a new online submission process for all tobacco reporting forms for the 2024 sales year. Companies are now able to submit tobacco licensee reports (Form TEU5), tobacco stamper reports (Form TEU10), and the Prevent All Cigarette Trafficking Act of 2009 (PACT Act¹) reports through new online forms. This modernized online submission process significantly reduces the administrative burden and streamlines the digital storage of these reports for the Unit.

The Unit sends formal demands to NPMs that have sales in Hawaii, requiring that they place appropriate sums in a qualified escrow fund in compliance with the Tobacco Liability Act. There have been no NPM sales in Hawaii since 2019, and therefore no escrow payments have been required since 2019. In 2021, one of the larger NPMs unsuccessfully attempted to be reinstated to the Hawaii directory. Soon after, the same company stopped selling NPM cigarettes nationwide.

¹ 18 U.S.C. § 1716E (2010).

E. 2003 Diligent Enforcement Arbitrations

The first major arbitration arising from the MSA was the 2003 DE Arbitration, which commenced in 2010 but did not conclude until 2013. In the 2003 DE Arbitration, Hawaii's diligent enforcement was not contested by the PMs, and Hawaii received its 2003 money, albeit years later. Twenty-four other states, along with Washington, D.C., and the Commonwealth of Puerto Rico, entered into an agreement with the PMs, the NPM Adjustment Settlement Agreement (NPMASA), settling the years 2003 through 2012. Several of the non-settling states won their 2003 arbitration hearings, and therefore "won" their disputed 2003 money (to be paid in 2014). Indiana, Kentucky, Maryland, Missouri, New Mexico, and Pennsylvania, however, were found to be non-diligent and lost their hearings. These six states suffered losses of expected annual MSA payments in 2014 and 2015 in amounts of approximately \$500 - \$600 million, although at least one state reduced some of the impact through court appeals.

F. 2004 Diligent Enforcement Arbitrations

Soon after the 2003 DE Arbitration ended, the 2004 DE Arbitration commenced. In 2017, after nearly two years of pretrial litigation and extensive discovery, the PMs affirmatively challenged Hawaii's diligent enforcement for the calendar year 2004. Hawaii's arbitration was scheduled to begin in August of 2018. In 2018, with the assistance of outside counsel, Hawaii and nine other states signed on to the NPMASA with the PMs, resolving the diligent enforcement arbitration issues for the years 2004 through and including 2017. By joining the settlement, Hawaii was spared the cost and uncertainty of ongoing and protracted arbitrations. It was estimated that, had Hawaii not settled the 2004 DE Arbitration, it would have cost Hawaii approximately \$1.5 million dollars in litigation costs alone just for the 2004 DE Arbitration – arbitrations covering each year from 2005 through 2017 would have been separate and more costly.²

In April 2018, Hawaii received approximately \$58.6 million for the settlement of the years 2004 through and including 2017. Outside litigation costs totaled approximately \$189,000. After Hawaii and nine other states joined the NPMASA, nine other states were still involved in the 2004 DE Arbitration. In September 2021, two arbitration panels issued decisions resolving liability for the 2004 DE Arbitration as to eight states. Six states (Idaho, Illinois, Iowa, Maryland, Ohio, and Wisconsin) were found to have diligently enforced. Two states (Missouri and Washington) were found to be non-diligent. In October 2022, a separate arbitration panel found New Mexico to be non-diligent. In August 2023, a New Mexico state court vacated the arbitration panel's decision. That decision is currently on appeal. If the arbitration panel's decision is held invalid on appeal, it is possible that New Mexico and PMs will have to return to commence arbitration for sales year 2024 anew. In 2023, the Independent Auditor that handles the annual MSA disbursements assessed the arbitration losses against

² Had Hawaii prevailed in the 2004 DE Arbitration, Hawaii would have received \$4,648,059.24, the amount withheld by the industry from the industry's 2004 payment to Hawaii, plus any interest that accrued on the withheld amount.

Missouri, New Mexico and Washington, and those three states received MSA distributions that were reduced by tens of millions of dollars combined.

The 2004 arbitration panels placed great emphasis on efforts the states made to perform audits, and this was a major factor in whether a state was found to be diligent or non-diligent. Based on the panel findings in the 2004 arbitration hearings, the Unit added an auditor in June 2023 to help ensure diligent enforcement efforts would remain robust.

G. 2005 Through 2007 Diligent Enforcement Arbitrations

Hearings for the 2005-2007 NPM adjustment arbitration for the remaining arbitrating states commenced in 2022. Despite both states having been found by the panels to have diligently enforced in 2004, Illinois signed onto the NPMASA in 2022, and Iowa signed on in 2023. In February 2024, Idaho also signed onto the NPMASA. In August 2024, Massachusetts settled with the PMs for NPM adjustments through 2011 and is also no longer involved in the 2005-2007 arbitration. Of the remaining arbitrating states, the panel has issued interim awards finding Maryland, Ohio, and Wisconsin diligent, but finding Washington non-diligent for 2005, 2006, and 2007. Subsequently, in 2025, Washington settled with all of the PMs except for Philip Morris USA Inc. (PM USA), one of the largest PMs. PM USA subsequently demanded arbitration, claiming that the settlement was invalid. This matter is still pending. Missouri's 2005 diligent enforcement hearing was held in June 2025, and the panel's decision is anticipated soon. New Mexico's 2004 diligent enforcement hearing has yet to be scheduled as of August 2025.

H. NPM Adjustment Settlement Agreements, 2018-2024

After joining the settlement in 2018, Hawaii still faced potential liability for future years of diligent enforcement arbitration from 2018 and into the future. If Hawaii had not settled years 2018 through 2022, Hawaii would have faced an estimated maximum exposure ranging from approximately \$17 million to \$21 million per year in lost MSA payments – comprising over half of the payments Hawaii could expect to receive in each year. In 2020, a condition of the NPMASA was met that automatically settled the years 2018-2019 for Hawaii and eight other states, thus protecting Hawaii from the risk of arbitration for diligent enforcement in those years. For the settled years, called "transition years," Hawaii and the other states retain seventy-five percent of the disputed payment amount, while the PMs receive a twenty-five percent credit. In addition, in future unsettled years, Hawaii's risk is limited to approximately half of what it would be if Hawaii had not joined the NPMASA. For example, if Hawaii had not joined the NPMASA and was found non-diligent for sales year 2022, it could have potentially lost the entire annual MSA payment received in 2023 - \$40.9 million. Because it signed the NPMASA, Hawaii was only at risk for approximately half of that amount.

In 2020, Hawaii joined the other states in its group opting to treat years 2020-2022 as transition years, another option available to these states as part of the

settlement signed in 2018. This option protected Hawaii from the risk of arbitration through sales year 2022. Also in 2020, Hawaii, along with thirty-four other states, the District of Columbia and Puerto Rico, entered into the 2018 through 2022 NPMASA with the PMs, providing Hawaii with additional benefits and protections for potential arbitration in the future. In March 2024, after extended negotiations, Hawaii and thirty-three other states, along with the District of Columbia and Puerto Rico, signed onto the 2023 and 2024 NPMASA, meaning that Hawaii was settled through sales year 2024 for arbitration relating to the NPM adjustment. Along with the District of Columbia and Puerto Rico, there are currently thirty-seven states that have signed onto versions of this agreement. Massachusetts, Montana, and New York have all entered separate settlements with the PMs resolving the NPM adjustment. In 2025, Washington entered a separate settlement, extending to 2031, with all the PMs except PM USA. That leaves only six states that are still arbitrating – Maryland, Missouri, New Mexico, Ohio, Washington (which is only partially settled), and Wisconsin.

In April 2024, Hawaii received its annual MSA payment in the amount of \$33,809,139.01, and payments are current, subject to some adjustments over time. Since Hawaii and most of the other states are only settled through sales year 2024, negotiations to settle future years, like those agreed to by recently settled states (Illinois, Idaho, and Iowa), are ongoing. Attorneys from the Unit are playing an integral role in these negotiations. If Hawaii does not settle future years and faces arbitration for sales year 2025 and beyond, it is unclear when that would commence, but it could possibly be several years away at this point, because the 2005 through 2007 arbitrations are ongoing. If, however, some of the arbitrating states settle quickly, Hawaii could be facing the risk of arbitration in the very near future.

III. CIGARETTE TAX AND TOBACCO TAX LAW (Chapter 245, HRS)

A. Background

In 2000, the Legislature recognized the need for a mandatory cigarette tax stamp system "to assess, collect, and enforce the cigarette and tobacco tax." The Conference Committee on S.B. No. 2486, S.D. 2, H.D. 2, C.D. 1 (2000) (Act 249, Session Laws of Hawaii 2000), reported:

[E]nforcement of the current system of collecting cigarette and tobacco taxes is sporadic, haphazard, and ineffective, resulting in uncollected potential tax revenue. The current system of filing of returns by licensed dealers is in effect a system of voluntary compliance. Persons may try to sell cigarettes and tobacco products without obtaining a license, or could have a license and not file a return or understate the income on the return.

The Legislature recognized that obtaining proof of large-scale black market cigarette sales is nearly impossible because the activity is surreptitious, and Hawaii's resources are limited. Nonetheless, the Legislature concluded, "judging from the anecdotal evidence existing and continuing over a fifteen-year period that a black

market exists." Conf. Comm. Rep. No. 98, in 2000 House Journal, at page 898; in 2000 Senate Journal, at page 776. With these concerns in mind, the Cigarette Tax and Tobacco Tax Law, chapter 245, HRS, was amended by Act 249 to require that the tax on the sale or use of cigarettes under section 245-3, HRS, shall be paid by licensees through the use of stamps. Beginning on January 1, 2001, a licensee or its authorized agent or designee has been required to affix a stamp to the bottom of each individual package of cigarettes prior to distribution. Beginning on April 1, 2001, no individual package of cigarettes could be sold or offered for sale to the public unless affixed with the stamp as required by chapter 245, HRS. Beginning in 2000, the Unit worked closely with licensed wholesalers and dealers and DOTAX to implement the cigarette stamp program. In January 2001, the Unit began conducting inspections for compliance with the program. The Unit continues to monitor the monthly licensee list, ensure that licensees are complying with reporting requirements, and work closely with DOTAX to ensure that licenses are revoked when appropriate.

In 2005, the Department proposed a bill to amend chapter 245, HRS, to require a permit for the retail sale of cigarettes and other tobacco products, and to require retailers to keep adequate records. These amendments became effective on December 1, 2006 (Act 131, Session Laws of Hawaii 2005). The retail tobacco permit program addresses the problem of cigarettes and other tobacco products being imported to Hawaii by entities other than known wholesalers and distributors; for example, consumers and retail stores often order cigarettes by Internet, telephone, or mail. The record-keeping requirements of the retail tobacco permit program help law enforcement officers determine the sources of cigarettes and other tobacco products sold at retail and help prevent evasion of state taxes. The Unit's investigators continue to ensure that retailers are complying with the requirements of the retail tobacco permit program, and if they find a retailer that is not in compliance, further action is taken to bring the retailer into compliance.

In 2023, the Department supported Senate Bill No. 975 (Act 62), which established the offense of unlawful shipment of tobacco products; amended the definition of "tobacco products" in chapter 245, HRS, to include and subject "electronic smoking device" and "e-liquid" to taxation and regulation under DOTAX; imposed an excise tax of seventy percent of the wholesale price of each ESD or e-liquid sold, used, or possessed by a wholesaler or dealer on and after January 1, 2024; increased the license and permit fees for wholesalers, dealers, and retailers of tobacco products; repealed chapter 28, part XII, HRS, relating to the Electronic Smoking Device Retailer Registration Unit under the Attorney General; and repealed section 245-17, HRS, relating to Delivery Sales. The bill was signed into law on June 6, 2023 (Act 62, Session Laws of Hawaii 2023). From the time the bill passed, the Unit has been working with the Department of Health, DOTAX, the Governor's Office, and members of the public to address the impact of Act 62.

B. Cigarette Tax Revenue Collections

Since the implementation of the tax stamp program on January 1, 2001, Hawaii has collected a total of \$2,449,085,805 in cigarette tax revenues. Cigarette tax revenue collections increased significantly through FY 2010-2011. At its peak in FY 2010-2011, revenues reached a high of \$135,647,918. From FY 2011-2012 until the present, however, cigarette tax revenue collections have decreased almost every year. In FY 2024-2025, DOTAX reported cigarette tax revenue collections of \$63,070,190, a reduction of ten percent from FY 2023-2024, and a reduction of fifty-four percent from FY 2010-2011.

This downward trend in cigarette tax revenue collections is expected to continue. The Unit's diligent enforcement efforts to comply with the MSA and statutory obligations will be impacted by this drastic decrease in funding, as most of the Unit's funding is derived from cigarette tax revenue collections. If the Unit is unable to maintain its diligent enforcement efforts, Hawaii's future annual MSA payments will be at risk. To address this issue, in 2023 and 2024, the Department proposed and supported several bills to stabilize funding for the Unit. On June 21, 2024, House Bill No. 982 was signed into law (Act 59, Session Laws of Hawaii 2024). Act 59 amended section 28-15(c), HRS, by increasing the amount of funds that the Special Fund can carry over from \$500,000 to \$750,000 at the end of the fiscal year; and amended section 328L-2(a), HRS, by increasing the sum of moneys received from the MSA annually from \$350,000 to \$750,000. On May 27, 2025, House Bill No. 441 was signed into law (Act 95, Session Laws of Hawaii 2025). Act 95 amended section 245-3(a), HRS, by increasing the cigarette tax from sixteen cents to eighteen cents; and amended section 245-15, HRS, amending the disposition of cigarette tax revenues by allocating the increase in the cigarette tax amount to the Hawaii cancer research special fund. The Unit anticipates that the Special Fund will receive additional revenue due to the increased cigarette tax.

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Cigarette Tax Revenue Collections by Fiscal Year

FY 1999-2000	\$ 40,049,539
FY 2000-2001	51,739,469
FY 2001-2002	62,609,477
FY 2002-2003	70,586,392
FY 2003-2004	77,541,843
FY 2004-2005	83,135,360
FY 2005-2006	85,702,483
FY 2006-2007	88,771,666
FY 2007-2008	101,560,051
FY 2008-2009	104,433,576
FY 2009-2010	119,926,741
FY 2010-2011	135,647,918
FY 2011-2012	130,994,721
FY 2012-2013	120,095,909
FY 2013-2014	114,112,465
FY 2014-2015	121,629,882
FY 2015-2016	116,382,902
FY 2016-2017	114,926,266
FY 2017-2018	110,762,991
FY 2018-2019	102,793,762
FY 2019-2020	102,444,639
FY 2020-2021	98,140,929
FY 2021-2022	85,131,574
FY 2022-2023	76,802,634
FY 2023-2024	70,092,426
FY 2024-2025	63,070,190
Total	\$2,449,085,805

C. Enforcement

The Unit conducts inspections, including unannounced inspections, of wholesalers and distributors, retail establishments, and cigarette vending machines for compliance with the Cigarette Tax and Tobacco Tax Law. The Unit also conducts investigations in coordination with federal agencies, resulting in seizures of contraband. The Unit also coordinates with DOTAX to monitor license holders and retail permit holders.

- As of July 2025, DOTAX reported that 1,198 retailers located in the State of Hawaii held retail tobacco permits: 741 in the City and County of Honolulu, 194 in the County of Hawaii, 181 in the County of Maui, and 77 in the County of Kauai. In FY 2024-2025, 1,690 compliance inspections were conducted statewide: 1,274 on Oahu, 227 on the island of Hawaii, 73 on Kauai, 102 on Maui, 0 on Lanai, and 14 on Molokai.

- As of July 2025, DOTAX reported 149 individuals and/or entities held tobacco licenses. Pursuant to Act 62, Session Laws of Hawaii 2023, starting July 1, 2023, wholesalers and dealers of ESDs and e-liquids are required to have a tobacco license with DOTAX. To prepare for the influx of these additional licensees, the Unit initiated new procedures to collaborate with DOTAX to monitor licensees, identify non-compliant entities, and take measures to either bring those entities into compliance or take steps to revoke their licenses.
- Since April 1, 2001, enforcement activities have resulted in more than 161 felony arrests, numerous investigations, and seizure of more than 3,501,788 illegal cigarettes and 291.58 pounds of tobacco leaves. Historically, arrests have been made on Hawaii, Kauai, Maui, Molokai, and Oahu.
- In FY 2024-2025, ten criminal tobacco investigations were conducted. A total of 255 cartons and seven packs of cigarettes (the equivalent of 51,140 cigarettes) were seized at the Daniel K. Inouye International Airport (three investigations), at the United States Post Office (six investigations), and by the State Fire Council (one investigation) as a result of cooperative efforts between the Department, United States Customs and Border Protection, Homeland Security, the United States Postal Service, and the State Fire Council.
- Since April 1, 2001, the Unit has prosecuted 139 tobacco cases, resulting in criminal fines of \$197,600. This data has not changed in the last year. When the MSA first went into effect there were many prosecutions, but with the MSA and the threat of prosecution, retailers came into compliance, and the Unit actively maintains compliance through inspections and education.
- In total, seventy-five cigarette prosecutions have resulted in court-ordered forfeiture of cigarettes. In addition, in ninety-nine instances, the Department secured forfeiture of confiscated cigarettes via civil administrative forfeiture orders, stipulations, or agreements. For the same reasons noted above, this data has not changed in the last year.

D. Gray Market

Gray market cigarettes are American-made or foreign-made cigarettes – usually major American brands – sold by the manufacturers specifically for sale outside of the United States that nevertheless end up in the United States. Gray market cigarettes cut into the market share of the PMs. Gray market cigarettes include cigarettes that have been imported illegally into the United States in violation of federal law, fail to meet federally mandated labeling requirements, or bear an unauthorized brand or trademark and are considered contraband. Foreign-made gray market cigarettes are

manufactured overseas in such places as China, Colombia, the Philippines, Southeast Asia, and Switzerland, representing a multitude of brands and cigarette manufacturers. These cigarettes are often smuggled into Hawaii from Asia (predominantly from the Philippines and Southeast Asia) and the South Pacific and have been found in small grocery and liquor stores. Some mainland distributors attempt to mask or re-label "Tax Exempt" cigarettes to avoid prosecution for sale of gray market cigarettes.

Historically, to address the gray market and other contraband cigarette problems, the Department has established relationships and has shared information with the taxing and regulatory authorities of Alaska, Arizona, California, Florida, Michigan, Oregon, Utah, Vermont, Washington, and Canada. The Department has also historically coordinated with the Bureau of Alcohol, Tobacco, Firearms, and Explosives; the Internal Revenue Service; United States Customs and Border Protection; the United States Postal Service; and the Royal Canadian Mounted Police regarding gray market cigarettes and other contraband cigarette-related issues. The Department has worked with United States Customs and Border Protection in joint investigations of persons smuggling contraband cigarettes to Hawaii from foreign countries.

E. Counterfeit Tax Stamps

Counterfeit tax stamps cost as little as \$0.03 to \$0.50 per stamp and, therefore, create a significant price advantage over vendors who sell properly stamped cigarettes. The Unit searches for counterfeit Hawaii tax stamps to prevent their circulation.

In FY 2022-2023, the Unit met with other states and worked with DOTAX to add additional security features to the stamps used in the cigarette tax stamp program. As a result of these efforts, DOTAX entered into a new contract with the stamp vendor which included stamps that, for the first time, had unique numbering, variable images, and microprint. In FY 2023-2024 and FY 2024-2025, DOTAX and the stamp vendor agreed to extend the contract for another year. The Unit continues to work with DOTAX and the stamp vendor to enable the vendor to ship stamps directly to distributors, as well as to implement additional security features to the stamps in the coming years.

F. Half-Stamping

Historically, vendors have attempted to evade the cigarette tax by placing a half-stamp on the bottom of a package of cigarettes, thus stamping two packs for the price of one. Investigations have resulted in arrests for selling half-stamped or partially stamped packs. In November 2001, the Unit made arrests for half-stamping and seized 12,879 packs, of which 2,639 packs were half-stamped and 10,240 packs were unstamped. The Unit continues to ensure that the application of tax stamps complies with the stamping requirements set forth by rules adopted by DOTAX.³

³ Section 18-245-3, Hawaii Administrative Rules, provides that stamps or stamping indicia shall be securely affixed to the bottom of each cigarette package in such a manner that the stamps or stamping indicia are clearly visible, legible, and complete.

G. Sales by Internet and Mail

Efforts continue in Hawaii and across the nation to address the problem of Internet sales of cigarettes. Significant federal regulation through the PACT Act was passed in March 2010. In March 2021, Congress amended the PACT Act to include new regulations regarding the delivery and sales of electronic nicotine delivery systems, which includes vapes and e-cigarettes and flavored and smokeless tobacco.

On a weekly basis, the Unit investigators make multiple checks for illegal online sales of tobacco products. In FY 2024-2025, the Unit investigators initiated three investigations into Craigslist internet offerings and one investigation into OfferUp for the sale of tobacco products without a tobacco retail permit within the State of Hawaii. The investigations resulted in listings being removed from Craigslist and OfferUp promptly after the investigations were initiated.

As noted above, interdiction activities also took place in conjunction with United States Customs and Border Protection and the United States Postal Service resulting in parcels of cigarettes and loose tobacco being seized as prohibited mailed items and treated as contraband in violation of the PACT Act.

Act 62, Session Laws of Hawaii 2023, established the offense of unlawful shipment of tobacco products, and amended the definition of "tobacco products" in chapter 245, HRS, to include and subject "electronic smoking device" and "e-liquid" to taxation and regulation under DOTAX. From the time the bill passed, the Unit has been working with the Department of Health, DOTAX, and other states to establish programs to address illegal online sales nationally and into Hawaii.

H. Other Current Activities

The Unit continues to work to address both current and ever-changing risks posed by cigarettes, e-cigarettes, and other new products like nicotine pouches. The Unit worked closely with other states and the NAAG Tobacco Center to take action against illegal vape products, often coming in illegally from China. One of the projects currently starting up involves working with multiple other states using internet stings to shut down distributors at the higher level of the distribution chain. During this fiscal year, the Unit played an active role in the Smoking in Movies and Streaming Working Group, working closely with the Coalition for a Tobacco-Free Hawai'i (CTFH) Youth Council. The CTFH Youth Council is a youth-led organization for students from eighth grade through college, from public and private schools representing six islands. Attorney General Anne Lopez, attorneys from the Unit, and members of the CTFH Youth Council met and worked together to advocate for the reduction of tobacco imagery in movies and streaming content, to protect youth from the harmful influence of onscreen tobacco use, and to promote healthier media environments.

IV. FY 2024-2025 RECEIPTS INTO THE TOBACCO ENFORCEMENT SPECIAL FUND

Master Settlement Agreement funds	\$ 750,000
Cigarette tax stamp fees/interest/fines/misc.	934,632
Total	\$1,684,632

V. FY 2024-2025 APPROPRIATIONS AND EXPENDITURES

In FY 2024-2025, there was a total appropriation of \$1,823,174.00 for the MSA and cigarette tax stamp enforcement. The appropriation was funded in part by \$750,000 from moneys received from the MSA and \$934,632 from cigarette tax stamp fees.

Expenses for FY 2024-2025 totaled \$1,123,750.50, which leaves an appropriation balance of \$699,423.50.

Looking to the future, current trends indicate that personnel costs will continue to rise, while cigarette tax revenues and MSA payments will continue to decrease. With the passage of Act 59, Session Laws of 2024, the Unit anticipates that the Special Fund will receive increased funding starting in early 2026. However, the Department must continue its attempts to secure additional revenue to stabilize the Unit's funding. This is necessary to continue the Unit's diligent enforcement efforts, thus reducing Hawaii's risk of losing future DE arbitrations and millions of dollars in future MSA payments.

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TOBACCO ENFORCEMENT SPECIAL FUND
Fiscal Year 2024-2025

APPROPRIATION		\$1,823,174.00
PERSONNEL COSTS		
Salaries and Fringe	\$912,942.45	
OPERATIONAL EXPENSES & OVERHEAD COSTS		
Supplies	109.94	
Membership Dues and Subscriptions	1,907.00	
Telephone	7,002.51	
Printing and Binding	0	
Mileage	668.77	
Travel Costs	6,568.82	
Lease Rent	78,303.53	
Rental of Equipment	6,605.77	
Repairs and Maintenance	125.65	
Special Fund Assessment for AG Department (Redistribute Expenses)	0	
Special Fund Assessments paid to B&F	109,516.06	
Total Operational Expenses & Overhead Costs	\$210,808.05	
TOTAL COSTS	\$1,123,750.50	
APPROPRIATION BALANCE		\$699,423.50