

# DEPARTMENT OF TAXATION

## 2012 Fiscal Impact Statement

1. **Patron** John C. Watkins

3. **Committee** Senate Finance

4. **Title** Roll-Your-Own Cigarette Machines;  
Manufacturers of Cigarettes

2. **Bill Number** SB 74

**House of Origin:**

  X   **Introduced**

       **Substitute**

       **Engrossed**

**Second House:**

       **In Committee**

       **Substitute**

       **Enrolled**

### 5. **Summary/Purpose:**

This bill would provide that any person who maintains or operates a “roll-your-own cigarette machine” at a retail establishment that enables a person to process a product that is made or derived from tobacco onto a roll or tube shall be deemed a manufacturer of cigarettes. The resulting product would be deemed a cigarette sold to a consumer for the purposes of the Virginia Cigarette Tax, the implementation of the Master Settlement Agreement, and reduced cigarette ignition propensity.

Under current law, roll-your-own tobacco is included in the definition of “cigarette” and subject to the Virginia Cigarette Tax at the rate of 10% of the manufacturer’s sales price. Currently, no cigarette may be sold in the Commonwealth unless the manufacturer has certified with the Department of Agricultural and Consumer Services that its ignition strength has been tested and met the performance standard set forth in the Code. The packaging of the cigarette must also be marked as being compliant with such fire safety standards and meet federal requirements related to the health effects of smoking.

The effective date of this bill is not specified.

6. **Budget amendment necessary:** No.

7. **Fiscal Impact Estimates are:** Not available. (See Line 8.)

### 8. **Fiscal implications:**

#### Administrative Costs

The Department considers implementation of this bill as routine, and does not require additional funding.

#### Revenue Impact

This bill would declare retail establishments that maintain or operate a roll-your-own cigarette machine to be manufacturers, which would result in the establishment being

required to pay the excise tax on cigarettes sold. The bill would also require such retail establishments to either become a participating manufacturer or pay into a qualified escrow fund pursuant to the implementation of the Master Settlement Agreement. To the extent that tobacco products not currently subject to the state and local cigarette tax would be subject to the cigarette taxes, this bill would result in an unknown increase in state and local revenues.

**9. Specific agency or political subdivisions affected:**

Department of Taxation  
Office of the Attorney General  
Department of Agricultural and Consumer Services  
State Fire Marshall

**10. Technical amendment necessary: Yes.**

If the intent of this bill is not to subject tobacco used in roll-your-own cigarette machines to Virginia Cigarette Tax at the per pack rate, the following technical amendment is suggested:

Page 1, Line 15, After a cigarette  
Insert: , but not roll-your-own tobacco,

If the intent of this bill is to subject products of roll-your-own cigarette machines operating by retail establishments to the local cigarette tax, the following technical amendment is suggested:

Page 1, Line 16, After this  
Strike: chapter  
Insert: title

If the intent of this bill is not to subject tobacco used in roll-your-own cigarette machines to the Virginia Cigarette Tax twice, the following technical amendment is suggested:

Page 1, Line 17, After 59.1.  
Insert: Tobacco purchased by such retail establishment for use in such a machine shall be exempt from taxation under this chapter.

**11. Other comments:**

Cigarette Tax

Pursuant to *Va. Code* § 58.1-1001, the Commonwealth imposes a state cigarette tax at the rate of 1.5 cents per cigarette (30 cents per pack of 20 cigarettes). The cigarette tax is paid by stamping agents through the purchase of stamps, which under *Va. Code* § 58.1-1003 must be affixed to each individual package, bag, box, or can from which cigarettes are sold. Currently, only manufacturers, wholesale dealers and retail dealers may be permitted as stamping agents. No person may purchase, possess or affix Virginia revenue stamps without first obtaining a permit to do so from the Department. In order to

obtain a stamping permit, a person must submit an application and application fee of \$600 to the Department, which conducts a background investigation on the applicant.

All cities and towns with general taxing powers are currently authorized to impose a cigarette tax with no rate limitations. Only two counties, Arlington and Fairfax, are authorized to impose a local cigarette tax under Va. Code § 58.1-3831, which is limited to the amount of the state cigarette tax rate. Both impose a local cigarette tax at the maximum rate of \$0.30 per pack of 20 cigarettes. Local cigarette taxes are typically administered and enforced at the local level. However, the Northern Virginia Cigarette Tax Board administers and enforces the local cigarette tax on behalf of 17 northern Virginia jurisdictions.

### Master Settlement Agreement

On November 23, 1998, leading United States tobacco product manufacturers, called participating manufacturers (PMs) entered into the Master Settlement Agreement (MSA) with the Commonwealth and 45 other states. The agreement obligated PMs, in return for release from past, present and certain future claims against them, to pay substantial sums to the Commonwealth. Tobacco product manufacturers who are not parties to the MSA, called nonparticipating manufacturers (NPMs), must pay sums into a qualified escrow fund from which claims may be paid if such manufacturers are determined in future years to have acted culpably. The escrow fund serves as a financial responsibility mechanism to guarantee a source of compensation and to prevent NPMs from becoming judgment-proof before liability may arise. The NPM statute must be diligently enforced to ensure a state is exempt from the application of the NPM adjustment contained in the MSA.

### Virginia's Nonparticipating Manufacturers Statute

The NPM Statute requires any tobacco product manufacturer selling cigarettes after July 1, 1999, who does not participate in the MSA to make deposits into a qualified escrow fund. The NPM statute also requires that each NPM certify to the Office of the Attorney General annually that it is in compliance with the statute.

Every tobacco product manufacturer whose cigarettes are sold in Virginia must certify annually to the Tax Commissioner and the Attorney General that it is a PM or NPM in compliance with the NPM statute. In addition to making this designation, each tobacco product manufacturer must include with its certification a list of brand families sold in Virginia. NPMs must also report detailed information on how many units of each brand were sold in the Commonwealth in the preceding year. Only brands covered under the MSA or in the NPM escrow fund may be certified. All manufacturers must maintain records necessary for the certification for a period of five years.

Any person who is authorized to affix stamps to cigarettes or required to pay the excise tax on cigarettes must submit monthly reports to the Department of Taxation that includes a list by brand of the number of cigarettes that such person affixed stamps to during the previous month. Stamping agents must also file a quarterly report with the Attorney General that includes a list by brand family of the total number of cigarettes for which the stamping agent affixed stamps during the previous calendar quarter or otherwise paid the

tax due for such cigarettes. Additionally, every tobacco product manufacturer whose cigarettes are to be sold in the Commonwealth shall either submit to the Attorney General a true and correct copy of the returns or reports it files or as required to file with the Alcohol and Tobacco Tax and Trade Bureau, United States Department of Treasury or submit a request or consent to the United States Department of Treasury to authorize the Alcohol and Tobacco Tax and Trade Bureau to disclose such returns to the Attorney General.

#### Reduced Cigarette Ignition Propensity

Beginning January 1, 2010, cigarettes may not be sold or offered for sale unless the cigarettes have been tested to determine that they meet a performance standard for fire safety regarding the likelihood that the cigarette will ignite material it may contact. Cigarette manufacturers are required to file a certification with the Commissioner of Agriculture and Consumer Services that their cigarettes meet the mandated performance standard as measured by the prescribed test. Cigarette packages are required to be marked so that compliant cigarettes may be distinguished from those not certified as compliant. The specific mark is determined by the manufacturer, subject to approval by the Commissioner of Agriculture and Consumer Services. Cigarettes compliant with similar New York regulations are compliant with the Virginia requirements and manufacturers may use the same package markings they use in New York. Violators are subject to a civil penalty of \$100 for each cigarette pack sold that is not in compliance with the performance standard, not to exceed \$100,000 for a manufacturer or other person selling cigarettes other than by retail sale for sales during any 30-day period and not to exceed \$25,000 for a retailer for sales during any 30-day period.

#### Opinion of the Attorney General

On September 2, 2011, the Attorney General held, in Opinion No. 11-095, that a retailer who allows customers to use an on-premises machine to make roll-your-own cigarettes for that customer's personal use was not a "tobacco product manufacturer" under the Virginia Escrow Statute. The Attorney General stated that a retailer does not directly manufacture the cigarettes and could not become a manufacturer indirectly based upon a consumer's use of the roll-your-own machines. Additionally, the Attorney General held that as cigarettes produced by roll-your-own machines are not intended to be sold but are for personal use, such cigarettes fall outside the scope of the statute's definition of "tobacco product manufacturers."

#### Proposal

This bill would provide that any person who maintains or operates a machine at a retail establishment that enables a person to process a product that is made or derived from tobacco onto a roll or tube, "roll-your-own cigarette machine", shall be deemed a manufacturer of cigarettes. The resulting product would be deemed a cigarette sold to a consumer for the purposes of the Virginia Cigarette Tax, the implementation of the Master Settlement Agreement, and reduced cigarette ignition propensity.

The effective date of this bill is not specified.

### Similar Legislation

**House Bill 314** is identical to this bill.

**House Bill 160** would increase the Cigarette Tax rate from \$0.30 per pack to \$1.45 per pack of 20 cigarettes and would increase the tax on roll-your-own tobacco from 10% to 50% of the manufacturer's sales price. The bill would also increase the Tobacco Products Tax on certain tobacco products from 10% to 50% of the manufacturer's sales price.

cc : Secretary of Finance

Date: 1/20/2012 AM  
DLAS File Name: SB74F161