

DEPARTMENT OF TAXATION

2015 Fiscal Impact Statement

1. **Patron** K. Rob Krupicka

3. **Committee** House Finance

4. **Title** Cigarette Tax and Tobacco Products Tax;
Increase

2. **Bill Number** HB 1590

House of Origin:

 X **Introduced**

 Substitute

 Engrossed

Second House:

 In Committee

 Substitute

 Enrolled

5. **Summary/Purpose:**

This bill would increase the Cigarette Tax rate from \$0.30 per pack to \$2.00 per pack of 20 cigarettes and would increase the tax on roll-your-own tobacco from 10% to 60% of the manufacturer's sales price. The bill would also increase the Tobacco Products Tax on loose leaf tobacco to rates of \$1.26 for each unit that is less than 4 ounces, \$2.40 for each unit that is at least 4 ounces but not more than 8 ounces, and \$4.20 for each unit more than 8 ounces but not more than 24 ounces. Units of loose leaf tobacco that exceed 24 ounces are subject to the Tobacco Products Tax at a rate of \$1.26 per unit plus \$1.26 for each 4 ounce increment that the unit exceeds 16 ounces. The bill would increase the Tobacco Products Tax on tobacco products other than moist snuff or loose leaf tobacco from 10% to 60% of the manufacturer's sales price.

The bill provides that the additional revenue attributable to the increased tax rates on cigarettes and roll-your own tobacco would be apportioned among all counties and cities based on school-age population and used for maintenance, operation, capital outlays, debt and interest payments, or other expenses incurred in the operation of the public schools, which shall be considered as funds raised from local resources. In any county having an incorporated town constituting a school division, the county treasurer shall pay into the town treasury an amount proportionate to the ratio the school population of such town bears to the school population of the entire county for maintenance, operation, capital outlays, debt and interest payments, or other expenses incurred in the operation of the public schools.

Under current law, the tobacco products tax is imposed on loose leaf tobacco at rates of \$0.21 for each unit that is less than 4 ounces, \$0.40 for each unit that is at least 4 ounces but not more than 8 ounces, and \$0.70 for each unit more than 8 ounces but not more than 24 ounces. Units of loose leaf tobacco that exceed 24 ounces are subject to the Tobacco Products Tax at a rate of \$0.21 per unit plus \$0.21 for each 4 ounce increment that the unit exceeds 16 ounces. Loose leaf tobacco is defined as any leaf tobacco that is not intended to be smoked, but does not include moist snuff.

The effective date of this bill is not specified.

6. Budget amendment necessary: Yes.

ITEM(S): Page 1, Revenue Estimates

301, Medicaid Program Services, Department of Medical Assistance Services

7. Fiscal Impact Estimates are: Preliminary. (See Line 8.)

7a. Expenditure Impact:

<i>Fiscal Year</i>	<i>Dollars</i>	<i>Positions</i>	<i>Fund</i>
2014-15	\$0	0	GF
2015-16	\$153,000	2	GF
2016-17	\$148,000	2	GF
2017-18	\$148,000	2	GF
2018-19	\$148,000	2	GF
2019-20	\$148,000	2	GF
2020-21	\$148,000	2	GF

8. Fiscal implications:

Administrative Costs

The Department would incur administrative expenses of approximately \$153,000 in Fiscal Year 2016 and \$148,000 in Fiscal Year 2017 and each Fiscal Year thereafter for two auditors in order to effectively enforce the cigarette and other tobacco products taxes.

On November 23, 1998, leading United States tobacco product manufacturers, called participating manufacturers entered into the Master Settlement Agreement with the Commonwealth and 45 other states. Compliance with the cigarette tax must be diligently enforced to ensure a state is exempt from the application of the NPM adjustment contained in the MSA. Significant increases in cigarette and tobacco products taxes may lead to an increase in the evasion of taxes. Additionally, this bill would increase the rate of Virginia's cigarette tax higher than the rate in neighboring states and change the Commonwealth from a cigarette export state to a cigarette import state, which would impact the Department's compliance efforts. This may result in a need for more compliance staff and resources in future years.

Revenue Impact

This bill would increase the Cigarette Tax and the Tobacco Products Tax on loose leaf tobacco and certain other tobacco products. The revenues attributable to the increase in the rates would be dedicated to the counties and cities of the Commonwealth. This bill is estimated to provide revenues of \$437.4 million in Fiscal Year 2016, \$478.1 million in Fiscal Year 2017, \$479.0 million in Fiscal Year 2018, \$480.0 million in Fiscal Year 2019, \$481.1 million in Fiscal Year 2020, and \$482.1 million in Fiscal Year 2021 in local revenues. The chart below shows the source of the revenues.

<p>HB 1590: Local Revenue Impact Increase in Cigarette Tax and OTP Tax</p>
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Effective July 1, 2015 (\$ Millions)						
	<u>FY2016</u>	<u>FY2017</u>	<u>FY2018</u>	<u>FY2019</u>	<u>FY2020</u>	<u>FY2021</u>
Cigarettes	\$402.6	\$439.2	\$439.2	\$439.2	\$439.2	\$439.2
Loose Leaf Tobacco	\$4.9	\$5.5	\$5.7	\$5.8	\$5.9	\$6.1
Certain Other Tobacco Products	\$29.9	\$33.4	\$34.2	\$35.0	\$36.0	\$36.8
Total	\$437.4	\$478.1	\$479.0	\$480.0	\$481.1	\$482.1

As fewer cigarettes, loose leaf tobacco, and certain other tobacco products are sold as the price increases, significantly increasing the tax on these products decreases the amount of such products that are sold. As the bill would dedicate the revenues attributable to the current rate of taxes to the Health Care Fund, decreasing the number of products sold also decreases the revenues dedicated to the Health Care Fund. This bill is estimated to decrease revenues to the Health Care Fund by \$71.0 million in Fiscal Year 2016, \$77.5 million in Fiscal Year 2017, \$77.6 million in Fiscal Year 2018, \$77.6 million in Fiscal Year 2019, \$77.7 million in Fiscal Year 2020, and \$77.8 million in Fiscal Year 2021. The chart below shows the source of the revenues.

HB 1590: Health Care Fund Revenue Impact Increase in Cigarette Tax and OTP Tax Effective July 1, 2015 (\$ Millions)						
	<u>FY2016</u>	<u>FY2017</u>	<u>FY2018</u>	<u>FY2019</u>	<u>FY2020</u>	<u>FY2021</u>
Cigarettes	(\$68.6)	(\$74.8)	(\$74.8)	(\$74.8)	(\$74.8)	(\$74.8)
Loose Leaf Tobacco	(\$2.1)	(\$2.4)	(\$2.4)	(\$2.5)	(\$2.6)	(\$2.6)
Certain Other Tobacco Products	(\$0.3)	(\$0.3)	(\$0.3)	(\$0.3)	(\$0.3)	(\$0.3)
Total	(\$71.0)	(\$77.5)	(\$77.6)	(\$77.6)	(\$77.7)	(\$77.8)

As the Retail Sales and Use Tax is imposed on the sale of cigarettes, the decrease in the number of cigarettes sold is estimated to decrease Retail Sales and Use Tax revenues by approximately \$48.1 million in Fiscal Year 2016, \$52.4 million in Fiscal Year 2017 and each Fiscal Year thereafter. However, even with a decrease in the number of loose leaf tobacco and certain other tobacco products sold, the increase in the price because of the tax increase is estimated to result in a increase in Retail Sales and Use Tax revenues of \$400,000 in Fiscal Year 2016, Fiscal Year 2017, Fiscal Year 2018, and Fiscal Year 2019 and \$500,000 in Fiscal Year 2020 and each Fiscal Year thereafter. In total, this bill would decrease revenues from the Retail Sales and Use Tax by approximately \$47.7 million in Fiscal Year 2016 and \$52.0 million in Fiscal Year 2017 and each Fiscal Year thereafter. The chart below shows the estimated Retail Sales and Use Tax revenue impact of the bill to each Fund.

HB 1590: State and Local Retail Sales and Use Tax Revenue Impact FY 2016-FY 2021 (\$ Millions)						
	<u>FY 2016</u>	<u>FY 2017</u>	<u>FY 2018</u>	<u>FY 2019</u>	<u>FY 2020</u>	<u>FY 2021</u>

GF Unrestricted	(\$19.1)	(\$20.9)	(\$20.9)	(\$20.8)	(\$20.8)	(\$20.8)
GF Restricted	(\$9.4)	(\$10.3)	(\$10.3)	(\$10.3)	(\$10.3)	(\$10.3)
Transportation Trust Fund	(\$9.9)	(\$10.8)	(\$10.8)	(\$10.8)	(\$10.8)	(\$10.8)
Local	(\$8.4)	(\$9.2)	(\$9.2)	(\$9.2)	(\$9.2)	(\$9.2)
HMOF	(\$0.8)	(\$0.9)	(\$0.9)	(\$0.9)	(\$0.9)	(\$0.9)
Total	(\$47.7)	(\$52.0)	(\$52.0)	(\$52.0)	(\$52.0)	(\$52.0)

9. Specific agency or political subdivisions affected:

Department of Taxation
Health Care Fund
All counties and cities

10. Technical amendment necessary: No.

11. Other comments:

Virginia Cigarette Tax

Virginia first imposed a state cigarette tax in 1960, at a rate of three cents per pack. A similar tax was also imposed on cigars. The tax rate on cigarettes remained at three cents per pack until 1966, when Virginia imposed a sales and use tax and simultaneously lowered the cigarette tax to 2.5 cents per pack. The tax on cigars was repealed in 1966. The cigarette tax increased to 20 cents per pack on August 1, 2004 and again on July 1, 2005 to 30 cents per pack. As of January, 1, 2015, Virginia is currently ranked as having the 50th lowest cigarette tax rate in the nation (including Washington, D.C.), only Missouri is ranked lower with a cigarette tax rate of 17 cents per pack.

State Excise Tax Rates on Cigarettes (Surrounding States)		
<u>State</u>	<u>Tax Rate</u>	<u>Rank</u>
Kentucky	\$0.60	40
Maryland	\$2.00	12
North Carolina	\$0.45	45
South Carolina	\$0.57	42
Tennessee	\$0.62	39
Virginia	\$0.30	50
West Virginia	\$0.55	44
Dist. Of Columbia	\$2.50	11

The Cigarette Tax is paid by wholesale dealers who have obtained a stamping agent permit from the Department of Taxation through the purchase of stamps, which must be affixed to each container from which cigarettes are sold. A discount equal to two percent of the purchase price of the Virginia revenue stamps is available to stamping agents.

Tobacco Products Tax

Prior to January 1, 2011, the tobacco products tax was imposed on tobacco products at the rate of 10% on the manufacturer's sales price. Cigarettes are not subject to the tax on tobacco products.

Tobacco products include the following:

- Cigars -- any roll of tobacco wrapped in leaf tobacco or in any substance containing tobacco (other than any roll of tobacco that is a cigarette).
- Smokeless tobacco --
 - Snuff -- any finely cut, ground, or powdered tobacco not intended to be smoked.
 - Chewing tobacco -- any leaf tobacco not intended to be smoked.
- Pipe tobacco -- any tobacco which, because of its appearance, type, packaging, or labeling, is suitable for use and likely to be offered to, or purchased by, consumers as tobacco to be smoked in a pipe.

Effective January 1, 2011, the tobacco products tax is imposed on moist snuff at a rate of \$0.18 per ounce based on net weight. Moist snuff is defined as any tobacco product consisting of finely cut, ground, or powdered tobacco that is not intended to be smoked but shall not include any finely cut, ground or powdered tobacco that is intended to be placed in the nasal cavity.

Effective January 1, 2011, the tobacco products tax is imposed on loose leaf tobacco at rates of \$0.21 for each unit that is less than 4 ounces, \$0.40 for each unit that is at least 4 ounces but not more than 8 ounces, and \$0.70 for each unit more than 8 ounces but not more than 24 ounces. Units of loose leaf tobacco that exceed 24 ounces are subject to the Tobacco Products Tax at a rate of \$0.21 per unit plus \$0.21 for each 4 ounce increment that the unit exceeds 16 ounces. Loose leaf tobacco is defined as any leaf tobacco that is not intended to be smoked, but does not include moist snuff.

The tax continues to be imposed on all other tobacco products at the rate of 10% on the manufacturer's sales price.

Health Care Fund

Under current law, all revenues from the Cigarette Tax, the tax on roll-your-own tobacco and the Tobacco Products Tax are deposited into the Health Care Fund. The federal government matches state funds spent on Medicaid, based on a state's federal medical assistance percentage (FMAP) match rate. The FMAP determined for each state has a statutory minimum of 50 percent and maximum of 83 percent; although Medicaid expenditures for some selected services and supports are matched at a higher rate for all states.

Currently, Health Care Fund revenues are used solely for the provision of health care services including, but not limited to, Medicaid payments, disease diagnosis, prevention and control, and community health services.

Proposal

This bill would increase the Cigarette Tax rate from \$0.30 per pack to \$2.00 per pack of 20 cigarettes and would increase the tax on roll-your-own tobacco from 10% to 60% of the manufacturer's sales price. The bill would also increase the Tobacco Products Tax on loose leaf tobacco to rates of \$1.26 for each unit that is less than 4 ounces, \$2.40 for each unit that is at least 4 ounces but not more than 8 ounces, and \$4.20 for each unit more than 8 ounces but not more than 24 ounces. Units of loose leaf tobacco that exceed 24 ounces are subject to the Tobacco Products Tax at a rate of \$1.26 per unit plus \$1.26 for each 4 ounce increment that the unit exceeds 16 ounces. The bill would increase the Tobacco Products Tax on tobacco products other than moist snuff or loose leaf tobacco from 10% to 60% of the manufacturer's sales price.

The bill provides that the additional revenue attributable to the increased tax rates on cigarettes and roll-your own tobacco would be apportioned among all counties and cities based on school-age population and used for maintenance, operation, capital outlays, debt and interest payments, or other expenses incurred in the operation of the public schools, which shall be considered as funds raised from local resources. In any county having an incorporated town constituting a school division, the county treasurer shall pay into the town treasury an amount proportionate to the ratio the school population of such town bears to the school population of the entire county for maintenance, operation, capital outlays, debt and interest payments, or other expenses incurred in the operation of the public schools.

The effective date of this bill is not specified.

Similar Legislation

House Bill 1310 would impose an excise tax on "vapor products" at the rate of \$0.40 per fluid milliliter of consumable product. The bill would also authorize any locality with the authority to impose a local cigarette tax to impose an excise tax on vapor products at a rate based upon the per milliliter content of consumable product in the vapor product.

Senate Bill 784 would authorize all counties, cities and towns to impose a local cigarette tax. Any county cigarette tax authorized by this bill would be limited to 5 cents per pack or the amount levied under state law, whichever is greater.

Senate Bill 1004 would impose an excise tax on "vapor products" at the rate of \$0.18 per fluid milliliter of consumable product. The bill would also authorize any locality with the authority to impose a local cigarette tax to impose an excise tax on vapor products at a rate based upon the per milliliter content of consumable product in the vapor product.

cc : Secretary of Finance

Date: 1/28/2015 AM
DLAS File Name: HB1590F161