DEPARTMENT OF TAXATION
2010 Fiscal Impact Statement

1. Patron David W. Marsden

2. Bill Number SB 701

House of Origin:
X **Introduced**
_____ **Substitute**
_____ **Engrossed**

Second House:
_____ **In Committee**
_____ **Substitute**
_____ **Enrolled**

3. Committee Senate Finance

4. Title Cigarette Tax; Fee Imposed on Nonparticipating Manufacturers

5. Summary/Purpose:

This bill would impose an annual fee on manufacturers that are not participating in the Master Settlement Agreement equal to the greater of i) $0.0225 for each cigarette that the Department of Taxation reasonably estimates that the manufacturer will sell between July 1, 2010 and December 31, 2010, or ii) $5,000, to be paid on or before September 1, 2010. For each year thereafter, the fee would be equal to the greater of i) $0.0225 for each cigarette that the Department of Taxation reasonably estimates that the manufacturer will sell in the calendar year, or ii) $10,000, to be paid on or before March 1. On or before the following April 15, the Department of Taxation would collect any fee due or refund any overpayment of the fee for the preceding year.

The effective date of this bill is not specified.

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

6a. Expenditure Impact:

Fiscal Year	***Dollars***	***Positions***	***Fund***
2009-10	$1,000	0	GF
2010-11	$388,000	3	GF
2011-12	$209,000	3	GF
2012-13	$212,000	3	GF
2013-14	$215,000	3	GF
2014-15	$218,000	3	GF
2015-16	$221,000	3	GF

6b.Revenue Impact:

Fiscal Year	***Dollars***	***Fund***
2010-11	$9.2 million	GF
	($1.9 million)	HCF
	($90,000)	TTF
	($170,000)	Local
2011-12	$9.2 million	GF
	($1.9 million)	HCF
	($90,000)	TTF
	($170,000)	Local
2002-13	$9.2 million	GF
	($1.9 million)	HCF
	($90,000)	TTF
	($170,000)	Local
2003-14	$9.2 million	GF
	($1.9 million)	HCF
	($90,000)	TTF
	($170,000)	Local
2014-15	$9.2 million	GF
	($1.9 million)	HCF
	($90,000)	TTF
	($170,000)	Local
2015-16	$9.2 million	GF
	($1.9 million)	HCF
	($90,000)	TTF
	($170,000)	Local

7. **Budget amendment necessary:** Yes.
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8. **Fiscal implications:**

Administrative Costs

TAX would incur administrative costs of $1,000 in Fiscal Year 2010, $388,000 in Fiscal Year 2011, $209,000 in Fiscal Year 2012, $212,000 in Fiscal Year 2013, $215,000 in Fiscal Year 2014, $218,000 in Fiscal Year 2015 and $221,000 in Fiscal Year 2016 for systems modifications, forms development, the printing and distribution of forms, forms processing and 2 auditors and 1 investigator for compliance and reporting purposes.

Revenue Impact

The revenue estimate for this bill assumes the elimination of the Cigarette Tax discount contained in the introduced Executive Budget.

The imposition of a $0.0225 per cigarette, or $0.45 per pack of 20 cigarettes, fee on cigarettes produced by nonparticipating manufacturers would generate approximately $9.8 million each year for the General Fund.

Because fewer cigarettes are sold as the price of cigarettes increases, this bill would result in a decrease in the number of cigarettes produced by nonparticipating manufacturers that are sold. Given the decrease in demand for the cigarettes, it is estimated that passage of this bill would decrease Cigarette Tax revenues to the Health Care Fund by approximately $1.9 million each year.

Additionally, as the Retail Sales and Use Tax is imposed on cigarettes, the decrease in the number of cigarettes sold would result in Retail Sales and Use Tax revenue decreasing by approximately $0.9 million each year. This revenue estimate assumes that the market share of nonparticipating manufacturers is 5.8%, based on 2008 data. If the market share of nonparticipating manufacturers is higher, the revenue estimate of this bill would be greater.

9. Specific agency or political subdivisions affected:

Department of Taxation

10. Technical amendment necessary: No.

11. Other comments:

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.

Other States

Legislation to impose a fee on nonparticipating manufacturers has been enacted in Michigan, Alaska, and Utah. However, in 2005, when similar legislation was passed by the Tennessee legislature, the Tennessee Attorney General stated that some large tobacco companies could interpret the new tax as violating the Master Settlement Agreement and withhold their payments as a result. Given the legal risks and the possibility that the payments would be delayed for several years in the event of a law suit, the Governor of Tennessee vetoed the legislation.

Proposal

This bill would impose an annual fee on manufacturers that are not participating in the Master Settlement Agreement an amount equal to the greater of $0.0225 for each cigarette that the Department of Taxation reasonably estimates that the manufacturer will sell in the year or $5,000 in Fiscal Year 2011. For Fiscal Year 2012 and each year thereafter, the fee would be equal to the greater of $0.0225 for each cigarette that the Department of Taxation reasonably estimates that the manufacturer will sell in the year or $10,000.

All nonparticipating manufacturers would be required to provide to the Department of Taxation information including the name, address, and telephone number of the nonparticipating manufacturer and its resident agent, the date it began or will begin selling cigarettes in the Commonwealth, and the brand names of the cigarettes that it is selling or will sell in the Commonwealth.

Cigarettes of a nonparticipating manufacturer that has not paid this fee would be treated as cigarettes of a nonparticipating manufacturer that has not provided the certification required under the NPM statute. In addition, persons permitted to stamp cigarettes would be barred from affixing stamps to such cigarettes. The Department of Taxation would be required to publish a list of all nonparticipating manufacturers that have complied with the requirements and paid the new fee.

The effective date of this bill is not specified.

Similar Legislation

House Bill 820 and **Senate Bill 476** would reduce and simplify the penalties related to unstamped cigarettes.

House Bill 889 would authorize all counties, cities and towns to impose a local cigarette tax. Any cigarette tax authorized by this bill would be limited to 5 cents per pack or the amount levied under state law, whichever is greater.

House Bill 891 would allow Isle of Wight County to levy a local cigarette tax in addition to the Counties of Arlington and Fairfax.

Senate Bill 578 would authorize all counties to impose a local cigarette tax at the state cigarette tax rate.

cc : Secretary of Finance

Date: 2/2/2010 AM
DLAS File Name: SB701F161