

DEPARTMENT OF TAXATION

2011 Fiscal Impact Statement

1. **Patron** Patrick A. Hope

3. **Committee** House Finance

4. **Title** Cigarette Tax; Increase

2. **Bill Number** HB 1815

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 \$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.

The bill provides that the additional revenue attributable to the increased tax rates on cigarettes and roll-your own tobacco would be appropriated as follows: 52% for Medicaid waivers for intellectual disabilities, 40% for Medicaid reimbursement to hospitals, 4% to the Virginia Department of Health for the state tobacco quitline, and 4% Virginia Healthy Youth Foundation to prevent tobacco use. The additional revenues attributable to the increased tax rate on certain other tobacco products would be dedicated to Medicaid waivers for intellectual disabilities.

The effective date of this bill is not specified.

6. **Budget amendment necessary:** Yes.

Item(s): Page 1, Revenue Estimates

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

8. **Fiscal implications:**

Administrative Costs

TAX has not assigned any administrative costs to this bill because the changes required by a single bill such as this can be implemented as part of the annual changes to our systems and forms. As stand-alone legislation, TAX considers implementation of this bill as "routine," and does not require additional funding.

TAX will provide specific administrative costs on any legislation that is not "routine." Additionally, TAX will review all state tax legislation likely to be enacted prior to the passage by each house. If the aggregate number of routine bills likely to pass either

house is unusually large, it is possible that additional resources will be required. If so, TAX will identify the costs at that time.

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 will typically lead to an increase in the evasion of taxes, which would impact TAX's compliance efforts and may result in an increase in costs for compliance staff and resources.

Revenue Impact

This bill would increase revenues to the Health Care Fund by approximately \$289.8 million dollars on an annual basis. Of the \$289.8 million, the tax increase on cigarettes would increase revenues by approximately \$261.3 million, the tax increase on roll-your-own tobacco would increase revenues by approximately \$800,000, and the tax increase on certain tobacco products would increase revenues by approximately \$27.8 million. The chart below shows the distribution of the revenues.

Because fewer cigarettes are sold as the price of cigarettes increases, this bill would result in a decrease in the number of cigarettes sold. As the Retail Sales and Use Tax is imposed on the sale of cigarettes, the decrease in the number of cigarettes sold would result in Retail Sales and Use Tax revenue decreasing by approximately \$36.4 million annually. Retail Sales and Use Tax revenues would increase by approximately \$5 million due to the increase in the tax on certain tobacco products. In total, this bill would decrease revenues from the Retail Sales and Use Tax by approximately \$31.3 million on an annual basis. The chart below shows the estimated revenue impact of the bill to each Fund:

Revenue Impact - \$1.15 Increase in Excise Tax on Cigarettes; Increase in the Tax on Roll Your Own Tobacco from 10% to 50%; Increase in Other Tobacco Products Excluding Moist Snuff and Loose Leaf (Millions of Dollars)				
	Cigarette Tax Increase	Roll Your Own Tax Increase	Tobacco Products Tax Increase	Total
Health Care Fund (Excise Tax Revenues)	\$261.3	\$0.8	\$27.8	\$289.8
Medicaid Waivers (52% of Cigarette and RYO, 100% of Tobacco Products)	\$135.9	\$0.4	\$27.8	\$164.1
Medicaid Reimbursements (40% of Cigarette and RYO)	\$104.5	\$0.3	\$0.0	\$104.8
VDH Tobacco Quitline (4% of Cigarette and RYO)	\$10.5	\$0.0	\$0.0	\$10.5
VA Healthy Youth Fund (4% of Cigarette and RYO)	\$10.5	\$0.0	\$0.0	(\$0.54)
Retail Sales and Use Tax Revenues	(\$36.4)	\$0.0	\$5.0	(\$31.3)
General Fund- Unrestricted	(\$18.2)	\$0.0	\$2.5	(\$15.7)
General Fund - Restricted	(\$7.2)	\$0.0	\$1.0	(\$6.2)
Transportation Trust Fund	(\$3.7)	\$0.0	\$0.5	(\$3.1)
Local Option	(\$7.3)	\$0.0	\$1.0	(\$6.3)

9. Specific agency or political subdivisions affected:

Department of Taxation
Virginia Health Care Fund

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. According to the Campaign for Tobacco-Free Kids, Key State-Specific Tobacco-Related Data and Rankings (December 1, 2010), 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	11
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	9

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.

Also 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, \$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 shall 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, the revenues from the Cigarette Tax are dedicated to the Health Care Fund and used solely for the provision of health care services including, but not limited, Medicaid payments, disease diagnosis, prevention and control, and community health services.

Proposal

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The bill provides that the additional revenue attributable to the increased tax rates on cigarettes and roll-your own tobacco would be appropriated as follows: 52% for Medicaid waivers for intellectual disabilities, 40% for Medicaid reimbursement to hospitals, 4% to the Virginia Department of Health for the state tobacco quitline, and 4% Virginia Healthy Youth Foundation to prevent tobacco use. The additional revenues attributable to the increased tax rate on certain other tobacco products would be dedicated to Medicaid waivers for intellectual disabilities.

The effective date of this bill is not specified.

Similar Legislation

House Bill 1750 would increase the Cigarette Tax rate from \$0.30 per pack to \$0.80 per pack of 20 cigarettes and would increase the tax on roll-your-own tobacco from 10% to 27% of the manufacturer's sales price.

House Bill 2038 and **Senate Bill 1085** would require local governing bodies to adopt ordinances that adhere to guidelines and rules established by the Department of Taxation related to cigarette tax enforcement.

House Bill 2138 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.

cc : Secretary of Finance

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