

Department of Legislative Services
Maryland General Assembly
2011 Session

FISCAL AND POLICY NOTE

Senate Bill 654

(Senator Forehand, *et al.*)

Budget and Taxation

Tobacco Tax - Rates and Distribution of Revenues

This bill increases the tobacco tax rate from \$2.00 to \$3.00 per pack; and the other tobacco product (OTP) tax rate from 15% to 95% of the wholesale price. In addition, the bill mandates specified minimum and maximum tax rates for certain other tobacco products. OTP tax revenue is redistributed from the general fund to a special fund to ensure that tobacco cessation programs receive at least \$21.0 million in annual funding beginning in fiscal 2013. Any additional money in the special fund is to be used to support Medicaid.

The bill takes effect July 1, 2011.

Fiscal Summary

State Effect: Net general fund revenues increase by \$53.4 million due to the increase in the cigarette tax, minus the loss of sales tax and OTP revenues. Special fund OTP tax revenues increase by \$40.4 million in FY 2012. Transportation Trust Fund (TTF) revenues decrease by \$0.4 million due to decreased sales tax revenues. OTP special fund expenditures increase by \$40.4 million in FY 2012 for Medicaid, with a corresponding decrease in general fund expenditures necessary to support the program. Future years reflect estimated OTP and cigarette tax revenues, OTP special fund expenditures specified by the bill, and decrease in Medicaid general fund expenditures.

(\$ in millions)	FY 2012	FY 2013	FY 2014	FY 2015	FY 2016
GF Revenue	\$53.4	\$50.5	\$47.6	\$44.8	\$41.8
SF Revenue	\$40.0	\$42.2	\$44.5	\$46.9	\$49.5
GF Expenditure	(\$40.4)	(\$31.6)	(\$34.0)	(\$36.4)	(\$39.1)
SF Expenditure	\$40.4	\$42.6	\$45.0	\$47.4	\$50.1
Net Effect	\$93.4	\$81.6	\$81.1	\$80.7	\$80.3

Note:() = decrease; GF = general funds; FF = federal funds; SF = special funds; - = indeterminate effect

Local Effect: None.

Small Business Effect: Meaningful.

Analysis

Bill Summary: The bill increases the tobacco tax from \$2.00 to \$3.00 per pack; and the OTP tax from 15% to 95% of the wholesale price. In addition, the bill mandates specified minimum and maximum tax rates for certain other tobacco products. The tax rate on other tobacco products is equal to:

- 95% of the wholesale price for cigars, not to exceed \$3.00 per cigar;
- the greater of 95% of the wholesale price or (1) \$3.00 per 1.2 ounce container of moist snuff tobacco; (2) 15 cents per dose of single dose smokeless tobacco; and (3) \$3.00 per 0.65 ounces of roll-your-own tobacco.

In addition, small-cigar cigarettes are taxed at the same rate as cigarettes. A small-cigar cigarette is defined as a small, thin cigar with the approximate dimensions of a cigarette or a cigarette wrapped in tobacco instead of paper.

The bill requires the Comptroller's Office to distribute OTP tax revenues to an OTP tax fund created by the bill. The fund may be used to provide additional funding for the State Tobacco Use Prevention and Cessation Program and ensure that the program receives at least \$21.0 million in total funding beginning in fiscal 2013. Any money expended from the fund to support the State Tobacco Use Prevention and Cessation Program is supplemental to and is not intended to take the place of funding that otherwise would be appropriated for this purpose. Any additional revenue remaining in the fund is required to fund Medicaid.

Current Law: Cigarettes are taxed at a rate of \$2.00 per pack. The discount rate on the purchase price of tobacco tax stamps offered by the Comptroller to cigarette wholesalers is 0.82%. OTP are taxed at a rate equal to 15% of the wholesale price. Cigarette and OTP revenues accrue to the general fund. The State is projected to collect \$408.7 million in total tobacco taxes in fiscal 2012.

In addition, the State sales tax of 6% is imposed on the final retail price of cigarettes and other tobacco products. A portion of sales tax revenues are distributed to TTF.

Background: Chapter 121 of 1999 increased the cigarette tax from \$0.36 to \$0.66 and also lowered the wholesaler discount from 1.36% to 0.82%. In addition, Chapter 121 imposed a 15% tax on the wholesale price of other tobacco products such as cigars and

smokeless tobacco. Chapter 288 of 2002 increased the cigarette tax from \$0.66 to \$1.00 per pack. Chapter 6 of the 2007 special session increased the cigarette tax to \$2.00 per pack. According to the Campaign for Tobacco-Free Kids, the average state cigarette excise tax imposed in the United States as of August 2010 was \$1.45 per pack. Combined with an average sales tax of 5.2%, total state taxes averaged \$1.70 per pack. Maryland imposed the eleventh highest cigarette excise tax and its combined sales and excise tax was twelfth highest. In fiscal 2010, of the total amount of OTP reported sold by wholesalers, 63% was cigars followed by moist snuff (25%), chewing tobacco (7%), roll-your-own (4%), and pipe tobacco (1%).

The Tobacco Use Prevention and Cessation Program aims to reduce the use of tobacco products and to reduce the burden of tobacco-related morbidity and mortality in the State. Under current law, mandated funding levels for tobacco use prevention and cessation programs in fiscal 2013 are scheduled to increase by \$4.0 million from 2012 levels (\$6.0 million to \$10.0 million).

However, over the past several years, the State's fiscal difficulties have prompted reductions to the mandated funding levels for various CRF programs. Most recently, the Budget Reconciliation and Financing Act of 2010 (Chapter 484) reduced CRF funding for tobacco use prevention and cessation activities to \$6.0 million in each of fiscal 2011 and 2012 and \$10.0 million annually beginning in fiscal 2013. Prior to these reductions, \$7.0 million was provided for these activities in fiscal 2011, and \$21.0 million was mandated for the activities in fiscal 2012 and beyond. The proposed fiscal 2012 State budget includes \$6.0 million in funding for the program, \$3.6 million of which is Cigarette Restitution Funds.

State Fiscal Effect: The bill increases the cigarette tax and OTP tax and redirects OTP tax revenues to support tobacco cessation programs and Medicaid. As a result, net general fund revenues increase by \$53.4 million in fiscal 2012 as shown in **Exhibit 1**. OTP special fund revenues increase by \$40.4 million in fiscal 2012 and TTF revenues decrease by \$0.4 million due to decreased sales taxes collected from other tobacco products and cigarettes.

Exhibit 1
SB 654 Fiscal Impact
Fiscal 2012-2016
(\$ in Thousands)

	<u>FY 2012</u>	<u>FY 2013</u>	<u>FY 2014</u>	<u>FY 2015</u>	<u>FY 2016</u>
Revenues					
<u>General Fund</u>					
OTP Revenues	(\$13,569)	(\$14,602)	(\$15,714)	(\$16,910)	(\$18,198)
Cigarette Tax	73,431	71,876	70,348	68,847	67,373
Sales Tax	(6,480)	(6,807)	(6,987)	(7,182)	(7,394)
Net General Fund	53,382	50,467	47,647	44,755	41,781
<u>Special Fund</u>					
OTP Revenue	40,405	42,628	44,972	47,446	50,055
TTF – Sales Tax	(363)	(473)	(486)	(499)	(514)
Total Revenues	\$93,425	\$92,621	\$92,134	\$91,701	\$91,322
Expenditures					
General Fund – Medicaid	(40,405)	(31,628)	(33,972)	(36,446)	(39,055)
OTP Fund	40,405	42,628	44,972	47,446	50,055
Tobacco Cessation	0	11,000	11,000	11,000	11,000
Medicaid	40,405	31,628	33,972	36,446	39,055
Total Expenditures	\$0	\$11,000	\$11,000	\$11,000	\$11,000
Net Impact	\$93,425	\$81,621	\$81,134	\$80,701	\$80,322

OTP special fund expenditures increase by \$40.4 million in fiscal 2012. The bill mandates that revenues from this fund ensure a total of \$21.0 million in annual tobacco cessation funding beginning in fiscal 2013. It is assumed that money that accrues to the fund in fiscal 2012 will support Medicaid. Although the bill specifies that funding for Medicaid is to be supplemental, additional special fund revenues will decrease the need for general fund expenditures in the program. Accordingly, special fund expenditures for Medicaid are assumed to offset general fund expenditures necessary to support the program. Beginning in fiscal 2013, \$11.0 million of OTP special fund revenues will be used to supplement tobacco cessation programs.

Small Business Impact: Small businesses that sell cigarettes and other tobacco products will be negatively impacted due to the decrease in the sales of these products resulting from the tax increases.

Additional Information

Prior Introductions: None.

Cross File: HB 853 (Delegate Hixson, *et al.*) - Ways and Means and Health and Government Operations.

Information Source(s): Comptroller's Office, Campaign for Tobacco-Free Kids, *Tax Burden on Tobacco*, Department of Legislative Services

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mc/jrb

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