

Department of Legislative Services
 Maryland General Assembly
 2020 Session

FISCAL AND POLICY NOTE
 First Reader

Senate Bill 233

(The President, *et al.*) (By Request - Office of the Attorney General)

Finance

Business Regulation - Flavored Tobacco Products - Prohibition

This emergency bill prohibits the manufacture, shipment, import, or sale of flavored tobacco products within the State. A violation is a misdemeanor punishable by maximum penalties of a \$1,000 fine and/or 30 days imprisonment. Further, the manufacture, shipment, import, or sale of (or attempt to manufacture, ship, import, or sell) a flavored tobacco product into or within the State constitutes doing business without an appropriate license; thus, a violation is a misdemeanor subject to existing penalties.

Fiscal Summary

State Effect: General fund revenues decrease by \$11.8 million in FY 2020 due to a reduction in tax revenues collected; future years reflect annualization and a projected decline in consumption. General fund expenditures for the Maryland Department of Health (MDH) increase by \$50,400 in FY 2020 only. Also, general fund revenues and expenditures increase to the extent penalties are imposed, beginning in FY 2020.

(in dollars)	FY 2020	FY 2021	FY 2022	FY 2023	FY 2024
GF Revenue	(\$11,796,000)	(\$69,372,000)	(\$70,731,000)	(\$72,034,000)	(\$73,287,000)
GF Expenditure	\$50,400	-	-	-	-
Net Effect	(\$11,846,400)	(\$69,372,000)	(\$70,731,000)	(\$72,034,000)	(\$73,287,000)

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

Local Effect: Montgomery County revenues may decrease significantly beginning in FY 2020 due to a decrease in e-cigarette excise tax revenues. Minimal increase in local government revenues and expenditures due to the bill’s penalty provisions. Enforcement by local health departments can be handled with existing resources.

Small Business Effect: Meaningful.

Analysis

Bill Summary:

Definitions

Tobacco Product: “Tobacco product” means a product intended for inhalation, absorption, ingestion, smoking, heating, chewing, dissolving, or any other manner of consumption by a human being and that is made of, derived from, or contains tobacco or nicotine. “Tobacco product” includes:

- cigarettes, cigars, pipe tobacco, chewing tobacco, snuff, snus, and any other tobacco product (OTP);
- electronic smoking devices (ESDs); and
- any component, part, or accessory of the above listed items regardless of nicotine content, including filters, rolling papers, blunt wraps, hemp wraps, hookahs, pipes, and liquids used in ESDs.

“Tobacco product” does not include a drug, device, or combination product authorized for sale by the U.S. Food and Drug Administration (FDA) under the federal Food, Drug, and Cosmetic Act.

Flavored Tobacco Product: “Flavored tobacco product” means a tobacco product that contains a taste or smell, other than that of tobacco, that is distinguishable by an ordinary consumer either before or during the consumption of the tobacco product. “Flavored tobacco product” includes a tobacco product with a taste or smell of fruit, menthol, mint, wintergreen, chocolate, cocoa, vanilla, honey, a candy, a dessert, an alcoholic beverage, an herb, or a spice.

Prohibition on Manufacture, Distribution, and Sale of Flavored Tobacco Products

A cigarette, OTP, or ESD license does not authorize the license holder to manufacture, ship, import, or sell into or within the State a flavored tobacco product. A public statement that a cigarette, OTP, or ESD has or produces a taste or smell other than tobacco is presumptive evidence that the cigarette is a flavored tobacco product if the statement is made by:

- the manufacturer;
- a person authorized by the manufacturer to make public statements about the cigarette, OTP, or ESD;

- a licensed wholesaler or a person authorized by the wholesaler to make public statements on the wholesaler’s behalf; or
- a licensed subwholesaler or a person authorized by the subwholesaler to make public statements on the subwholesaler’s behalf.

A violation is a misdemeanor punishable by a fine of up to \$1,000 and/or imprisonment for up to 30 days.

In addition, the manufacture, shipment, import, or sale of or attempt to manufacture, ship, import, or sell a flavored tobacco product into or within the State constitutes doing business without an appropriate cigarette, OTP, or ESD license, as prohibited under existing law. Accordingly, a violation is a misdemeanor punishable by a fine of up to \$1,000 and/or imprisonment for up to 30 days. Each day that a violation continues is a separate offense.

Furthermore, a person may not sell or dispense or offer to sell or dispense a flavored tobacco product through a vending machine in the State. A violation is a misdemeanor subject to an existing maximum fine of \$100.

Current Law:

Definitions

Tobacco Product: Chapter 396 of 2019 altered the definition of “tobacco product” as it applies to provisions of the Business Regulation Article governing tobacco product vending machines and provisions of the Criminal Law, Health-General, and Local Government articles. “Tobacco product,” as it applies to specified provisions, means a product that is intended for human inhalation, absorption, ingestion, smoking, heating, chewing, dissolving, or any other manner of consumption that is made of, derived from, or contains tobacco or nicotine. “Tobacco product” includes cigarettes, cigars, pipe tobacco, chewing tobacco, snuff, and snus; ESDs; and filters, rolling papers, pipes, and liquids used in ESDs, regardless of nicotine content. “Tobacco product” excludes a drug, device, or combination product authorized for sale by FDA under the federal Food, Drug, and Cosmetic Act.

ESDs: In addition, Chapter 396 renamed “electronic nicotine delivery system” (or ENDS) to be “electronic smoking device” and defined “electronic smoking device” as a device that can be used to deliver aerosolized or vaporized nicotine to an individual inhaling from the device. ESD includes (1) an electronic cigarette, an electronic cigar, an electronic cigarillo, an electronic pipe, an electronic hookah, a vape pen and vaping liquid, and (2) any component, part, or accessory of such a device regardless of whether or not it is sold separately, including any substance intended to be aerosolized or vaporized during use of

the device. ESD excludes a drug, device, or combination product authorized for sale by FDA under the Food, Drug, and Cosmetic Act.

Tobacco Licensing and Regulation

The Business Regulation Article governs the licensing of cigarette, OTP, and ESD manufacturers, wholesalers, retailers, storage warehouses, and vending machine operators. The Comptroller's Office issues manufacturer, wholesaler, storage warehouse, and vending machine operator licenses. However, effective June 1, 2020, this responsibility is transferred to the Alcohol and Tobacco Commission (ATC) established under Chapter 12 of 2019, as discussed in further detail below. The clerks of the circuit courts issue retail licenses.

With limited exception, a person may not act, attempt to act, or offer to act as (1) a cigarette manufacturer, retailer, storage warehouse, subwholesaler, vending machine operator, or wholesaler; (2) an OTP manufacturer, retailer, storage warehouse, wholesaler, or tobacconist; or (3) an ESD manufacturer, retailer, wholesaler distributor, wholesaler importer, or vape shop vendor without an appropriate license. A violation is a misdemeanor punishable by a fine of up to \$1,000 and/or imprisonment for up to 30 days. Each day that a violation continues is a separate offense.

Recent federal legislation raised the minimum age for an individual to purchase or be sold tobacco products from 18 to 21.

Monitoring and Enforcement

The Comptroller's Office is generally responsible for monitoring and enforcement activity related to tobacco and other business licenses. The Field Enforcement Division within the Comptroller's Office enforces State revenue and licensing laws pertaining to alcohol, tobacco, trader's, and transient vendor's licenses, the sales and use tax, and motor fuel, among others.

Chapter 12 of 2019, which takes effect June 1, 2020, establishes ATC and transfers duties of the Field Enforcement Division pertaining to alcohol and tobacco enforcement to ATC. The Comptroller's Office, however, retains duties related to enforcement of alcohol and tobacco taxes.

Background:

Tobacco Product Taxes

Cigarettes are taxed at a rate of \$2.00 per pack. Generally, the tax rate for OTPs is 30% of the wholesale price, which is the price for which a wholesaler buys OTPs, exclusive of any discount, trade allowance, rebate, or other reduction. The tax rate for cigars is 70% of the wholesale price of the cigars. The tax rate for premium cigars is 15% of the wholesale price of the premium cigars. OTP is defined as any cigar or roll for smoking, other than a cigarette, made in whole or in part of tobacco or any other tobacco or product made primarily from tobacco, other than a cigarette, that is intended by smoking or chewing or as a snuff.

Cigarette and OTP tax revenues accrue to the general fund. In fiscal 2021, cigarette tax revenues are projected to total \$299.0 million, and OTP tax revenues are projected to total \$42.6 million. In addition, the State sales and use tax rate of 6% is imposed on the final retail price of cigarettes and OTPs.

ESDs and their components are subject to the State sales and use tax but are not subject to a State excise tax. Montgomery County imposes a 30% tax on the wholesale value of vaping products. Montgomery County estimates that the tax generated \$1.3 million in fiscal 2019 and projects that revenues will total \$1.9 million in fiscal 2020.

Consumption of Menthol Cigarettes and Other Flavored Tobacco Products

According to a recent study by the U.S. Department of Health and Human Services, consumption of flavored and menthol tobacco products is significantly higher in Maryland than in the rest of the nation. For example, menthol cigarettes comprised about 44% of all cigarettes consumed in the State, compared to a national average of about one-third. In Maryland, flavored and menthol tobacco products comprised an estimated 40% to 60% of cigars and cigarillos and about three-quarters of moist snuff tobacco. The Comptroller's Office advises that it does not collect data on the percentage of tobacco taxes collected from flavored or menthol products.

Rise in Youth Use of E-cigarettes

According to the National Youth Tobacco Survey, in 2018, 1 in 5 high school students (20.8%) and 1 in 20 middle school students (4.9%) reported using electronic cigarettes (e-cigarettes) at least once in the previous 30 days, an increase of 78% and 48% since 2017, respectively. Among high school students currently using e-cigarettes, use of flavored e-cigarettes increased by 11.3% from 2017 to 2018. The 2019 Monitoring the Future Survey also found significant increases in youth vaping, noting that vaping among

grades 8, 10, and 12 more than doubled from 2017 to 2019. According to FDA, increased youth vaping is likely attributable to the popularity of USB-flash-drive-like e-cigarettes that have a high nicotine content, appealing flavors, and the ability to be easily concealed and used discreetly.

State Action to Restrict Access to Flavored E-cigarette Products

In response to alarming health concerns related to e-cigarette use, several states have taken action through emergency regulations or rulemaking to ban or restrict the sale of flavored e-cigarette products.

As of January 2020, two states – Massachusetts and New Jersey – have enacted legislation banning the sale of flavored vaping products. The Massachusetts legislation, signed into law in November 2019, restricts the sale and consumption of flavored nicotine vaping products and flavored cigarettes and other tobacco products (as defined in that state), including menthol cigarettes and flavored chewing tobacco, to licensed smoking bars, among other things. The New Jersey legislation, signed into law in January 2020, bans the sale and distribution of flavored vaping products, including menthol flavored products.

For more information on policies to address youth vaping, see [*Issue Papers, 2020 Legislative Session*](#), Department of Legislative Services (DLS), pgs. 79-81 (“Addressing Youth Vaping”) (December 2019).

Federal Action to Restrict Flavored E-cigarette Products

On January 2, 2020, FDA announced a policy to ban some, but not all, flavored e-cigarettes. According to FDA, the policy is intended to limit the rise in the use of e-cigarettes by teens – who overwhelmingly prefer flavors – while balancing the potential benefits to adults who already smoke flavored products other than tobacco and menthol.

The policy prohibits the production, distribution, and sale of all flavored cartridge-based e-cigarettes, with the exception of menthol and tobacco flavors, after February 1, 2020. After that date, a manufacturer must show that an unauthorized flavored cartridge is “appropriate for the protection of public health” and receive FDA approval.

The regulation applies to cartridges, or disposable pods, that are enclosed units that hold vaping liquid, which when heated in an e-cigarette is aerosolized into a breathable vapor. The policy does not apply to tank-style vapes, which are larger and run on refillable e-liquids that are customizable at vape shops.

State Revenues: General fund revenues decrease by an estimated \$11.8 million in fiscal 2020 due to lost tobacco product and sales tax revenues under the bill’s prohibition, as shown in **Exhibit 1**. This estimate assumes the bill takes effect May 1, 2020.

Exhibit 1
State Revenue Impacts of the Bill
Fiscal 2020-2024
(\$ in Millions)

	<u>FY 2020</u>	<u>FY 2021</u>	<u>FY 2022</u>	<u>FY 2023</u>	<u>FY 2024</u>
Cigarette tax	(\$7.7)	(\$44.8)	(\$45.3)	(\$45.8)	(\$46.1)
OTP tax	(2.0)	(11.8)	(12.3)	(12.9)	(13.5)
Sales and use tax	(2.2)	(12.7)	(13.1)	(13.4)	(13.7)
Total Revenues	(\$11.8)	(\$69.4)	(\$70.7)	(\$72.0)	(\$73.3)

OTP: other tobacco product

Notes: Numbers may not sum to total due to rounding. Fiscal 2020 revenue impacts reflect two months of impact only, assuming the bill takes effect May 1, 2020.

Source: Department of Legislative Services

This estimate (1) is based on the estimated percentage of menthol and flavored products consumed in the State in calendar 2015 and (2) assumes that most individuals who consume these products substitute other taxable tobacco products that are not affected by the bill. For example, based on research examining the impact of a similar policy restriction enacted in Ontario, Canada, it is assumed that the bill decreases the consumption of taxable cigarettes in the State by approximately 15% in fiscal 2020 and 2021. Future years reflect further declines in consumption.

To the extent that individuals do not substitute other taxable tobacco products, revenue losses are greater. It is estimated that the taxes imposed on flavored and menthol tobacco products would generate total revenues of \$183.6 million in fiscal 2021. Further, to the extent the bill takes effect sooner than May 1, 2020, revenues losses in fiscal 2020 are greater.

DLS advises there is considerable uncertainty about the impact the recent FDA restrictions on the sale of certain flavored vaping products will have on consumption of these products and, therefore, the potential revenue losses that would be observed in the absence of the bill.

Revenues losses are offset minimally to the extent the bill's monetary penalty provision and expanded application of existing monetary penalty provisions result in increased general fund revenues. Any such impact, however, is anticipated to be minimal.

State Expenditures: General fund expenditures for MDH increase by an estimated \$50,390 in fiscal 2020 only for the department to update training and educational materials for tobacco retailers and local health departments. Costs reflect necessary mailings and modification to enforcement and educational materials.

General fund expenditures increase further as a result of the bill's incarceration penalty and expanded application of an existing incarceration penalty to the extent more people are committed to State correctional facilities for convictions in Baltimore City. Any such impact, however, is anticipated to be minimal.

The Comptroller's Office and, when established, ATC can enforce the bill's provisions with existing resources.

If the bill results in reduced tobacco use-related health care costs covered by Medicaid, general fund expenditures decrease. Medicaid-eligible services are subject to a federal match rate (which varies depending on the coverage group of the individual). Therefore, federal fund expenditures also decrease, and federal fund revenues decrease correspondingly. However, DLS advises that this impact cannot be reliably quantified at this time, as it depends on whether and to what extent the bill reduces tobacco, OTP, and ESD use in the State.

Local Revenues: As noted above, Montgomery County imposes a 30% tax on the wholesale value of vaping products, which generated \$1.3 million in fiscal 2019 and is estimated to generate \$1.9 million in fiscal 2020. Under the bill, Montgomery County tax revenues decline beginning in fiscal 2020. The amount of the decline depends on the decrease in vaping products sold as a result of the bill, beyond the decrease that will result from FDA's recent regulatory action on these products.

Local Expenditures: Expenditures increase as a result of the bill's incarceration penalty and expanded application of an existing incarceration penalty. Counties pay the full cost of incarceration for people in their facilities for the first 12 months of the sentence. Per diem operating costs of local detention facilities have ranged from approximately \$40 to \$170 per inmate in recent years.

Small Business Effect: Sales decline, significantly in some cases, for small businesses in Maryland that sell flavored tobacco products. According to data provided by the Judiciary (Administrative Office of the Courts), in fiscal 2019, there were roughly 6,700 active

cigarette retailer licenses, 6,600 active OTP retailer and tobacconist licenses, and 170 active ESD (formerly ENDS) retailer and vape shop vendor licenses in the State.

Additional Information

Prior Introductions: None.

Designated Cross File: HB 3 (Delegate D.E. Davis) - Economic Matters and Health and Government Operations.

Information Source(s): Maryland Association of County Health Officers; Comptroller's Office; Judiciary (Administrative Office of the Courts); Maryland Department of Health; Montgomery County; states of Massachusetts and New Jersey; U.S. Food and Drug Administration; U.S. Department of Health and Human Services; Campaign for Tobacco Free Kids; *Nicotine & Tobacco Research*; *NPR*; *The Capital*; Department of Legislative Services

Fiscal Note History: First Reader - February 5, 2020
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