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TO: The Honorable Josaline Pena-Melnyk
Chair, Health and Government Operations Committee

FROM: John M. Leovy
Assistant Attorney General, Office of the Attorney General

RE: House Bill 1173 – Business Regulation – Tobacco Product Manufacturers –
Escrow Act – Alterations.

The Office of Attorney General urges this Committee to report favorably on House Bill 1173 – Business Regulation – Electronic Smoking Devices Manufactures – Certifications.

House Bill 1173 restores fairness and equity to Maryland's cigarette market. It amends Maryland's Tobacco Product Manufacturers Escrow Statute by removing a provision that allows companies that did not join the Master Settlement Agreement, or "MSA," to use their escrow accounts to subsidize low cigarette prices and undersell their competitors. House Bill 1173 will thus fulfill the legislature's intention when it enacted the Escrow Act, Bus. Reg. §§ 16-401–403, creating a level playing field for all the cigarette companies that compete in Maryland's market.

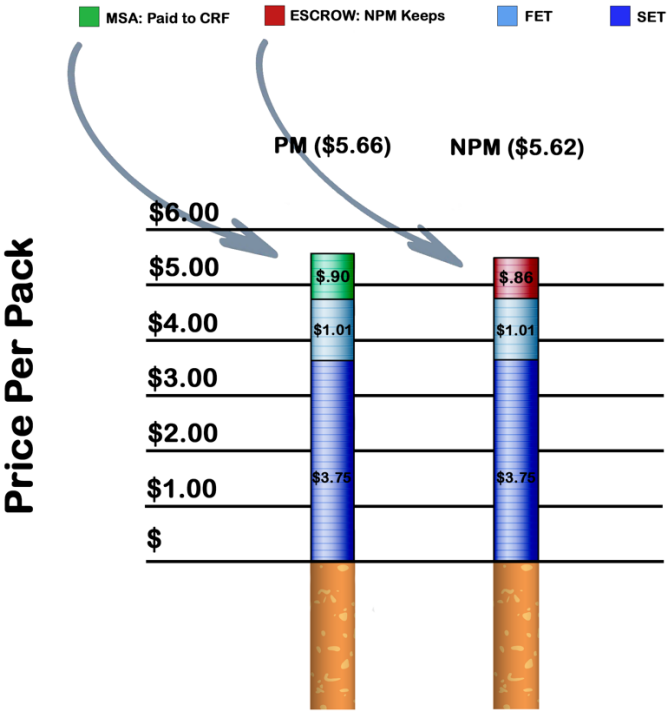
Maryland enacted the Escrow Act in 1999, the year after it signed the MSA. Cigarette companies that joined the MSA, called Participating Manufacturers ("PMs"), must end almost all cigarette advertising and pay Maryland and other States billions of dollars every year. These payments are to compensate the States for the past and future medical expenses incurred from treating their residents for the diseases cigarettes cause. As a result, Participating Manufacturers must raise their prices to finance their settlement payments. This creates a market opportunity for companies that do not join the MSA, called Nonparticipating Manufacturers ("NPMs"), to undersell the PMs.

This bill letter is a statement of the Office of Attorney General's policy position on the referenced pending legislation. For a legal or constitutional analysis of the bill, Members of the House and Senate should consult with the Counsel to the General Assembly, Sandy Brantley. She can be reached at 410-946-5600 or sbrantley@oag.state.md.us.

Intending to level the playing field between the PMs and the NPMs, Maryland and other States enacted the Escrow Act, which requires all cigarette companies to make a choice. They must either become a PM and comply with its financial obligations or remain an NPM and deposit funds into an escrow account roughly equal to the settlement payments that they would have to make to the State and leave the funds there for 25 years.

In the last 25 years, NPMs have collectively deposited more than \$10 million in escrow accounts for the cigarettes they have sold in Maryland. NPM cigarettes make Marylanders just as sick, and strain Maryland’s health care system, just as much as the PMs’ cigarettes do. The NPMs’ escrow accounts are assets held by the NPMs, which expect to recover every penny 25 years after they deposit it. NPMs also earn interest on the money in their escrow accounts, which they use to underwrite their business and sell cigarettes at prices lower than the PMs can. As one NPM recently boasted, they use the interest “to offset business expenses.”

The chart below illustrates why the current law favors NPMs and why the legislature needs to establish equity in the cigarette market by enacting HB 1173.



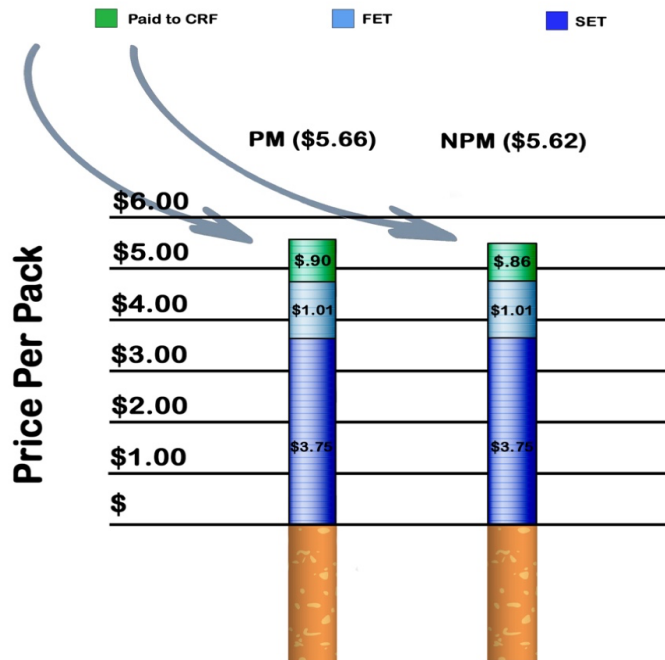
Both packs of cigarettes, PM and NPM, are subject to the same amount of Federal Excise Tax and State of Maryland Excise Tax. Where they differ is in that top level. The PMs pay about 90 cents per pack pursuant to the MSA and the money goes to Maryland’s Cigarette Restitution

Fund. But the NPMs deposit about 86 cents per pack and the money goes not to Maryland, but into an escrow account owned by the NPM, and they use the money, including interest earned, to subsidize their low-priced cigarettes. Those cheaper cigarettes drive up Maryland's smoking rate and cost Maryland's taxpayers more money treating people sickened and killed by NPM cigarettes.

The 25-year roll-out period will start soon, and the escrow accounts, which were intended to impose costs on NPMs and make funds available to States should they bring certain claims against NPMs, are now subsidizing low-priced cigarettes. This leaves Maryland's taxpayers to foot the bill for the costs associated with the NPMs' cigarettes. House Bill 1173 will put an end to this plan by restoring the level playing field between PMs and NPMs that Maryland's legislature intended when it first enacted Maryland's Escrow Act almost 25 years ago.

HB 1173 is also carefully drafted to avoid any risk to the State's future MSA settlement payments. If any future court or tribunal determines that the amendments contained in House Bill 1173 are unconstitutional or otherwise invalid, it provides that the current statute immediately snaps back in place as if it had not been amended.

The most important feature of HB 1173 is that it requires NPMs to pay the same amount of money they now use to underwrite their cigarette business to the State of Maryland instead. The amount of money at stake will not significantly impact the NPMs because the dollar amounts at issue in Maryland are relatively small, amounting to less than a million dollars a year based on 2023 data. But what HB 1173 will do is achieve the goals the legislature set for itself 25 years ago, and bring equity cigarette marketplace that is now out of balance. The chart below illustrates what will happen if the legislature enacts HB 1173:



By enacting House Bill 1173, Maryland can restore equity in Maryland's cigarette by creating the level playing field that the legislature intended when it enacted Maryland's Escrow Act a quarter of a century ago. The Office of the Attorney General strongly urges a favorable report on House Bill 1173.