

Department of Legislative Services
Maryland General Assembly
2009 Session

FISCAL AND POLICY NOTE

House Bill 680
Economic Matters

(Delegate Schuh, *et al.*)

Commercial Law - Maryland Cigarette Sales Below Cost Act - Cost to Retailer
and Wholesaler

This bill changes how the cost of cigarettes is determined by altering the statutory definitions of “basic cost of cigarettes” and “cost to the retailer” in the Maryland Cigarette Sales Below Cost Act. The basic cost of cigarettes is changed to mean the invoice or replacement cost of cigarettes. The cost to the retailer is derived by adding the retailer’s cost of doing business, which is assumed to be 8% of the basic cost of cigarettes, to the invoice or replacement cost of the cigarettes.

The bill also removes the definition of “cost to wholesaler” and the special cost provisions for wholesalers and retailers provided in statute.

Fiscal Summary

State Effect: None. The change does not materially affect State finances, but enforcement activity may be modified.

Local Effect: Any increase in the judicial workload of the circuit courts can be handled with existing resources.

Small Business Effect: Potential minimal. Small businesses may sell cigarettes for a slightly lower price.

Analysis

Current Law: The basic cost of cigarettes means the lesser of the invoice cost or the replacement cost of cigarettes to the retailer or wholesaler, including in-freight charges not reflected in the invoice or replacement cost minus any trade discount received. The

basic cost of cigarettes for wholesalers may include the full face value of any State cigarette taxes paid. Under certain circumstances, the presumptive wholesale or retail cost may be reduced.

The Cigarette Sales Below Cost Act prohibits a retailer or wholesaler with intent to injure a competitor or destroy or substantially lessen competition from:

- selling cigarettes below cost;
- selling cigarettes in combination with any merchandise if the other merchandise is given free of charge or sold at a price below cost;
- selling cigarettes in combination with any other merchandise if the total sale price is less than cost to the retailer or wholesaler of the cigarettes and the retail or wholesale cost of all other items included in the sale, including items given free of charge in connection with the sale;
- giving cigarettes free of charge, except in the case of specially packaged manufacturers' samples; or
- making any rebate, advertising allowance, or any other concession in connection with the sale of cigarettes whereby the cigarettes are effectively sold below cost.

In addition, a retailer may not purchase cigarettes from a wholesaler at a cost that directly or indirectly is less than the cost to the wholesaler by any means, including offering, accepting, or attempting to induce a rebate in price or concession in connection with the cigarette sale.

The prohibition against the sale of cigarettes below cost does not apply if the sale is made in good faith to meet competition; as part of a final liquidation or closing of the business; as imperfect, damaged, or discontinued cigarettes; as part of a bona fide clearance sale; or under the direction or order of a court.

The Comptroller is required to enforce compliance with the Act and calculate minimum costs as specified in the Act. On complaint of the Comptroller or any person affected, a circuit court has the authority to enjoin a retailer or wholesaler from the commission of any act prohibited by the Act and award damages and costs. The Comptroller is required to suspend or revoke the cigarette licensee of any person who violates the Act.

Under the Sales Below Cost Act, a retailer or wholesaler (of any good) with intent to injure a competitor or to destroy competition may not advertise, offer to sell, or sell at retail sale or wholesale sale any item of merchandise at less than its cost to the retailer or its cost to the wholesaler, respectively. On complaint from a person who claims to be injured from the action, a circuit court may issue an injunction against a retailer or wholesaler who is found to be engaging in selling merchandise below cost as prohibited.

Except with respect to combination sales and concessions, the Sales Below Cost Act does not apply to cigarette sales.

Background: The Comptroller's Office advises that a rise in complaints for violations of the Act may occur because the wholesale cost for cigarettes is altered to be the invoice cost only, and thus it is lower than under current law. Currently, the cost to wholesalers can be reduced by trade discounts and increased by the cigarette tax plus a 5% mark-up.

Because the bill allows a reduction in the wholesale cost of cigarettes, cigarette wholesalers in the State may sell cigarettes at a price that is actually lower than the price the company paid. By specifying that the "basic cost of cigarettes" is only the invoice or replacement cost, and allowing for other costs – such as in-freight charges or taxes paid – to be excluded, cigarette wholesalers may be able to sell cigarettes below cost without violating the Cigarette Sales Below Cost Act. Thus, large wholesalers that may be more able to incur short-term losses may benefit. The Comptroller's Office advises that there were 79 wholesalers in the State who sold nearly 2 billion packs of cigarettes in fiscal 2008; however, 61.5% of this market was controlled by the top 5 wholesalers.

State Fiscal Effect: According to the Comptroller's Office, there have been four complaints of violations of the Act so far in fiscal 2009, and eight complaints in fiscal 2008. None of these complaints resulted in a violation. The circuit courts have jurisdiction to impose damages or issue an injunction related to the Act. The Comptroller's Office advises that the increase in number of complaints does not materially affect the workload of the circuit courts.

Additional Information

Prior Introductions: None.

Cross File: SB 770 (Senator Astle) - Finance.

Information Source(s): Comptroller's Office, Judiciary (Administrative Office of the Courts), Office of the Attorney General (Consumer Protection Division), Department of Legislative Services

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