

Department of Legislative Services
Maryland General Assembly
2014 Session

FISCAL AND POLICY NOTE

Senate Bill 589 (Senator Jones-Rodwell, *et al.*)
Budget and Taxation and Finance

Tobacco Taxes - Healthy Maryland Initiative

This bill increases the tobacco tax rate from \$2.00 to \$3.00 per pack and the other tobacco product (OTP) tax rate from 30% to 95% of the wholesale price except for certain OTPs. The bill also requires the Governor to include at least \$21 million in annual funding for the Tobacco Use Prevention and Cessation Program beginning in fiscal 2016.

The bill takes effect July 1, 2014.

Fiscal Summary

State Effect: Net general fund revenues increase by \$110.8 million in FY 2015 due to the increase in the cigarette and OTP tax, minus the loss of sales tax revenues. General fund expenditures increase by \$11.0 million annually beginning in FY 2016, reflecting mandated tobacco cessation program funding. Future year estimates reflect projected tax revenue increases and mandated general fund expenditures. **This bill establishes a mandated appropriation beginning in FY 2016.**

(\$ in millions)	FY 2015	FY 2016	FY 2017	FY 2018	FY 2019
GF Revenue	\$110.8	\$111.2	\$111.0	\$110.7	\$110.3
GF Expenditure	\$0	\$11.0	\$11.0	\$11.0	\$11.0
Net Effect	\$110.8	\$100.2	\$100.0	\$99.7	\$99.3

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 rate from \$2.00 to \$3.00 per pack and the OTP tax rate from 30% to 95% of the wholesale price except for certain OTPs. The tax rate on OTPs is equal to:

- 95% of the wholesale price, not to exceed \$3.00 per cigar, for cigars with a wholesale price of less than \$20, or 15% of the wholesale price for cigars with a wholesale price of \$20 or greater;
- the greater of 95% of the wholesale price or \$3.00 per 0.65 ounces of roll-your-own tobacco;
- \$3.00 per 1.2 ounce or less container of conventional moist snuff smokeless tobacco (and proportionate amount of tax thereafter); and
- \$2.25 for each container of 15 doses or less of single-dose smokeless tobacco and 15 cents for each dose in a container of more than 15 doses.

In addition, small-cigar cigarettes are taxed at the same rate as regular 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 Governor to include at least \$21 million in annual funding for the Tobacco Use Prevention and Cessation Program beginning in fiscal 2016.

Current Law: Cigarettes are taxed at a rate of \$2.00 per pack. OTP are taxed at 30% of the wholesale price for all products, except cigars. The tax rate for cigars that are classified as premium cigars equals 15% of the wholesale price; all other cigars are taxed at 70% of the wholesale price. Cigarette and OTP tax revenues accrue to the general fund. In addition, the State sales tax rate of 6% is imposed on the final retail price of cigarettes and OTPs. Cigarette tax revenues are estimated to total \$371.5 million and OTPs tax revenues are estimated to total \$40.5 million in fiscal 2015.

Background: Chapter 121 of 1999 increased the cigarette tax from 36 cents to 66 cents. In addition, Chapter 121 imposed a 15% tax on the wholesale price of OTP such as cigars and smokeless tobacco. Chapter 288 of 2002 increased the cigarette tax from 66 cents to \$1.00 per pack. Chapter 6 of the 2007 special session increased the cigarette tax to \$2.00 per pack. 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 tobacco (4%), and pipe tobacco (1%).

Chapter 2 of the 2012 first special session increased the OTP tax rate from 15% to 30% of the wholesale price for all products except cigars effective July 1, 2012. The tax rate for cigars that are classified as premium cigars remained at 15% of the wholesale price; all other cigars are taxed at 70% of the wholesale price.

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. Over the past several years, the State’s fiscal difficulties have prompted reductions to the mandated funding levels for various programs funded by the Cigarette Restitution Fund. The Budget Reconciliation and Financing Act of 2010 (Chapter 484) reduced annual appropriations for tobacco use prevention and cessation activities to \$6 million in each of fiscal 2011 and 2012 and \$10 million annually beginning in fiscal 2013. Prior to these reductions, \$21.0 million was mandated for the activities annually. The Governor’s proposed fiscal 2015 State budget includes \$10.6 million in funding for the program.

Exhibit 1 shows the cigarette and OTP tax rates imposed in Maryland and surrounding states as of January 1, 2014, and the tax rate for moist snuff tobacco in those states that provide for a separate tax.

Exhibit 1
Cigarette, OTP, and Moist Snuff Tobacco Tax Rates in Surrounding States

<u>State</u>	<u>Cigarette Tax Rate</u>	<u>OTP Tax Rate</u>	<u>Moist Snuff Tobacco (per Ounce)</u>
Delaware	\$1.60	15%	\$0.54
District of Columbia	2.50 ¹	12% ²	0.75
Maryland	2.00	30% ³	
Pennsylvania	1.60	None	
Virginia	0.30 ⁴	10% ⁵	0.18
West Virginia	0.55	7%	

¹Also imposes an in lieu cigarette sales tax calculated annually and currently equal to \$0.36.

²Applied to retail price of certain products.

³Tax rate on premium cigars is 15% of the wholesale price and 70% of the wholesale price for all other cigars.

⁴Counties may impose an additional tax on cigarettes of \$0.02 to \$0.15.

⁵Applied to manufacturing price, chewing tobacco taxed per unit.

Source: Federation of Tax Administrators; Tobacco Free Kids Campaign

State Fiscal Effect: The bill increases the cigarette and OTP tax rates and requires the Governor to include at least \$21 million in annual funding for the Tobacco Use Prevention and Cessation Program beginning in fiscal 2016. As a result, general fund revenues increase by \$110.8 million in fiscal 2015, as shown in **Exhibit 2**.

Future year estimates reflect estimated net increases in general fund revenues and an increase of \$11.0 million in general fund expenditures to ensure a total of \$21.0 million in annual tobacco cessation program funding. The Department of Health and Mental Hygiene (DHMH) advises that it would hire six additional employees to conduct additional tobacco cessation initiatives, evaluations, and related expenditures.

The revenue estimates are based on past cigarette tax increases in Maryland and an examination of the additional OTP revenues generated through tax increases in 11 other states in fiscal 2006 through 2010, adjusted for Maryland. Based on these experiences, the estimates assume a significant reduction in the taxable consumption of cigarettes and OTPs following the tax increases.

Exhibit 2
Fiscal Impact of Legislation
Fiscal 2015-2019
(\$ in Millions)

	<u>FY 2015</u>	<u>FY 2016</u>	<u>FY 2017</u>	<u>FY 2018</u>	<u>FY 2019</u>
General Fund Revenues					
Cigarette Tax	\$76.1	\$75.0	\$73.8	\$72.5	\$71.0
OTP Revenues	40.5	41.7	42.8	\$44.0	45.3
Sales Tax	-5.8	-5.4	-5.6	-5.8	-6.0
Net General Fund	\$110.8	\$111.2	\$111.0	\$110.7	\$110.3
General Fund Expenditures					
Tobacco Cessation	\$0	\$11.0	\$11.0	\$11.0	\$11.0
Net Impact	\$110.8	\$100.2	\$100.0	\$99.7	\$99.3

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

Additional Information

Prior Introductions: Similar legislation was introduced in the 2011, 2012, and 2013 sessions. SB 700 of 2013 received a hearing in the Senate Budget and Taxation Committee, but no further action was taken. Its cross file, HB 683, received a hearing in the House Ways and Means and Health and Government Operations committees, but no further action was taken. SB 526 of 2012 received a hearing in the Senate Budget and Taxation Committee, but no further action was taken. Its cross file, HB 1153, received a hearing in the House Ways and Means Committee, but no further action was taken. SB 654 of 2011 received an unfavorable report from the Senate Budget and Taxation Committee. Its cross file, HB 853, received a hearing in the House Ways and Means Committee, but no further action was taken.

Cross File: HB 443 (Delegate Luedtke, *et al.*) - Ways and Means and Health and Government Operations.

Information Source(s): Department of Health and Mental Hygiene, Comptroller's Office, Federation of Tax Administrators, Tobacco Free Kids Campaign, Department of Legislative Services

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ncs/jrb

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