

**Department of Legislative Services**  
Maryland General Assembly  
2020 Session

**FISCAL AND POLICY NOTE**  
**Third Reader - Revised**

House Bill 3

(Delegate D.E. Davis)

Economic Matters and Health and  
Government Operations

Finance

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**Business Regulation – Tobacco Products – Electronic Smoking Devices,  
Prohibition on Flavoring, and Sales to Military Members**

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This bill prohibits the manufacture, sale, and distribution of cigarettes with “characterizing flavors,” including menthol, and restricts the retail sale and consumption of other tobacco products (OTPs) with “characterizing flavors” to “smoking bars.” However, premium cigars, with or without “characterizing flavors,” are excluded from the bill’s restrictions. The bill further prohibits the manufacture, sale, and distribution of closed and cartridge-based electronic smoking devices (ESDs) and generally prohibits the direct sale or shipment of ESDs to a consumer by mail or electronic network. Violations of the bill’s provisions are subject to various criminal penalties and/or disciplinary action. In addition, the bill conforms provisions of State law to the federal minimum age of 21 for an individual to purchase or be sold tobacco products by repealing specified exemptions for active-duty military members. The bill’s provisions are severable. **The bill takes effect January 1, 2021.**

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**Fiscal Summary**

**State Effect:** General fund revenues decrease by \$34.5 million in FY 2021 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 2021 only. Also, general fund revenues and expenditures increase to the extent penalties are imposed, beginning in FY 2021.

(\$ in millions)	FY 2021	FY 2022	FY 2023	FY 2024	FY 2025
GF Revenue	(\$34.48)	(\$70.30)	(\$71.59)	(\$72.82)	(\$74.01)
GF Expenditure	\$0.05	-	-	-	-
Net Effect	(\$34.53)	(\$70.30)	(\$71.59)	(\$72.82)	(\$74.01)

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

**Local Effect:** Montgomery County revenues likely decrease significantly beginning in FY 2021 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.

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## Analysis

**Bill Summary:** The bill establishes specified findings of the General Assembly related to the increase in the use of cartridge-based and closed ESDs by the State's youth population and the harm of such devices to the State's youth. The bill further establishes the intent of the General Assembly to discourage the use of such devices without depriving the adult users of ESDs of access to open ESD products as an alternative to combustible cigarettes.

### *Definitions*

**Characterizing Flavor:** "Characterizing flavor" means a distinguishable taste or aroma, other than the taste or aroma of tobacco, imparted or detectable before or during consumption of a tobacco product. It includes a taste or an aroma of any fruit, candy, dessert, alcoholic beverage, herb, or spice, including chocolate, vanilla, honey, cocoa, menthol, mint, or wintergreen. "Characterizing flavor" does not include any ingredient, including any additive or flavoring, that does not contribute to the distinguishable taste or aroma of the product.

**Smoking Bar:** "Smoking bar" means a retail tobacco establishment (1) that is primarily engaged in the retail sale of premium cigars, pipe tobacco, or OTPs for on-premises consumption; (2) in which the sale of other products is incidental; and (3) that primarily occupies an enclosed indoor space.

**Cartridge-based ESD:** "Cartridge-based ESD" means an ESD that consists of, includes, or involves a cartridge or pod that holds liquid that is to be aerosolized through product use. It includes an ESD that includes a cartridge, a pod, or any small enclosed unit, sealed or unsealed, that is designed to fit within or operate as part of an ESD.

**Closed ESD:** "Closed ESD" means an ESD, whether disposable, rechargeable, or reusable, that is sealed and prefilled with vaping liquid in a container that affixes directly to the battery or heating mechanism of the ESD (such as a disposable e-cigarette).

**Open ESD:** "Open ESD" means an ESD that has a tank, reservoir, or other container for vaping liquid that can be manually filled and refilled with vaping liquid.

### *Prohibition on Manufacture, Distribution, and Sale of Flavored Cigarettes and OTPs*

A cigarette license does not authorize the license holder to manufacture, ship, import, or sell into or within the State a cigarette that has a characterizing flavor (including menthol). With an exception for premium cigars, an OTP license does not authorize the license holder to manufacture, ship, import, or sell into or within the State an OTP that has a characterizing flavor *for off-premises* consumption. The bill's provisions may not be interpreted to prohibit the holder of an OTP license from manufacturing, shipping, importing, or selling into or within the State (1) premium cigars with or without a characterizing flavor for on- or off-premises consumption or (2) pipe tobacco or any OTP with a characterizing flavor for on-premises consumption at a smoking bar.

A public statement that a cigarette or an OTP has or produces a taste or smell other than tobacco is presumptive evidence that the cigarette or an OTP has a characterizing flavor if the statement is made by, as relevant to the product:

- the manufacturer;
- a person authorized by the manufacturer to make public statements about the cigarette or OTP;
- a licensed wholesaler or a person authorized by the wholesaler to make public statements on the wholesaler's behalf;
- a licensed subwholesaler or a person authorized by the subwholesaler to make public statements on the subwholesaler's behalf;
- a storage warehouse licensee or a person authorized by the licensee to make public statements on the licensee's behalf;
- a licensed retailer or a person authorized by the retailer to make public statements on the retailer's behalf; or
- a licensed tobacconist or a person authorized by the tobacconist to make public statements on the tobacconist'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 into or within the State of (1) a cigarette that has a characterizing flavor or (2) an OTP with a characterizing flavor, other than premium cigars, for off-premises consumption, constitutes doing business without an appropriate 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.

#### *Restrictions on the Manufacture, Distribution, and Sale of ESDs*

An ESD license does not authorize the holder to manufacture, ship, import, or sell into or within the State a cartridge-based or closed ESD. The manufacture, shipment, import, or sale of a cartridge-based or closed ESD into or within the State, or the attempt thereof, constitutes doing business without an appropriate 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.

In addition, a person who is engaged in the business of selling or distributing ESDs generally may not sell, ship, or cause to be shipped ESDs directly to a consumer or other unlicensed recipient in the State by mail or through a computer network. A licensed ESD retailer may, however, deliver up to two ESDs directly to a consumer if the delivery is made by the licensed ESD retailer or an employee of the licensee. A licensee who violates these restrictions is guilty of a misdemeanor and subject to a fine of up to \$1,000 and/or imprisonment for up to 30 days. In addition, a violation subjects a licensee to disciplinary action, as provided under existing law. An *unlicensed* person who commits a violation is guilty of a *felony* and is subject to a fine of up to \$50 for each ESD transported and/or imprisonment for up to two years.

#### **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 the U.S. Food and Drug Administration (FDA) under the federal Food, Drug, and Cosmetic Act.

*ESDs:* In addition, Chapter 396 renamed “electronic nicotine delivery system” (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.

### *Minimum Age*

Chapter 396 of 2019 generally raised the minimum age for an individual to purchase or be sold tobacco products from 18 to 21 with specified exceptions for active-duty military members at least age 18 who present valid military identification. Recent federal legislation, however, raised the federal minimum age for a person to purchase or be sold tobacco products from 18 to 21 *without exception*.

The distribution of tobacco products to underage individuals (under State law, an individual younger than age 21 or younger than age 18, if an active-duty member of the military) is generally prohibited under provisions of the Criminal Law and Health-General articles. A violator is subject to various civil or criminal penalties. Chapter 396 of 2019 authorized MDH to conduct unannounced inspections of licensed tobacco retailers to ensure compliance with minimum age provisions and other specified requirements of State law.

### *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. Pursuant to Business Regulation § 16.7-102, any person licensed under Title 16 (cigarettes) or 16.5 (OTPs) of the Business Regulation Article is authorized to manufacture, distribute, or

sell ESDs in the same capacity as the person is licensed under that title and is not required to obtain an additional ESD license.

A person who unlawfully manufactures, distributes, or sells tobacco products without an appropriate license is guilty of 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.

*Direct Sale of Tobacco Products to Consumers via Mail or Electronic Network*

A person generally may not sell or ship cigarettes directly to a consumer through the mail or an electronic network. However, a licensed cigarette retailer may deliver up to two cartons of cigarettes directly to a consumer if the delivery is made by the licensed retailer or an employee of the licensed retailer.

Similarly, a person generally may not sell or ship OTPs directly to a consumer through the mail or an electronic network. A licensed OTP retailer or tobacconist may deliver up to two packages of OTPs directly to a consumer if the delivery is made by the licensee or an employee of the licensee. The prohibition does not apply, however, to the order, purchase, sale, or shipment of premium cigars or pipe tobacco by a licensed OTP retailer or tobacconist.

A violation of these provisions is a felony subject a fine of up to \$50 for each carton of cigarettes or package of OTPs unlawfully sold or shipped and/or up to two years imprisonment. A licensee who commits a violation is subject to disciplinary action by the Comptroller (beginning June 1, 2020, ATC).

Chapters 199 and 200 of 2018 repealed a specific prohibition against the sale of ENDS by an ENDS retailer to a consumer through the mail or an electronic network. (As discussed above, Chapter 396 of 2019 renamed “electronic nicotine delivery systems,” or ENDS, to be “electronic smoking devices,” or ESDs, and otherwise defined ESD.) State law expressly authorizes a licensed ESD manufacturer to sell ESDs directly to a consumer if the consumer purchases or orders the devices through the mail or an electronic network.

*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.

### *Other 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.

*Recent Action by the Comptroller's Office to Restrict Flavored E-cigarette Products*

On February 10, 2020, the Comptroller announced action to prohibit the sale of certain disposable flavored ESDs not covered by the recent FDA policy. According to the Comptroller's Office, FED is prioritizing enforcement action against cartridge-based and disposable ESDs with flavors other than tobacco or menthol.

In October 2019, the Comptroller created the e-facts Task Force on Electronic Smoking Devices to study the public health and safety impacts of ESDs and to recommend regulatory and legislative action. The task force issued its final [report](#) on February 17, 2020.

**State Revenues:** General fund revenues decrease by an estimated \$34.5 million in fiscal 2021 due to lost tobacco product and sales tax revenues under the bill's provisions, as shown in **Exhibit 1**.

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**Exhibit 1**  
**State General Fund Revenue Impacts of the Bill**  
**Fiscal 2021-2025**  
**(\$ in Millions)**

	<b><u>FY 2021</u></b>	<b><u>FY 2022</u></b>	<b><u>FY 2023</u></b>	<b><u>FY 2024</u></b>	<b><u>FY 2025</u></b>
Cigarette tax	(\$22.4)	(\$45.3)	(\$45.8)	(\$46.1)	(\$46.4)
OTP tax	(5.7)	(11.9)	(12.5)	(13.0)	(13.6)
Sales tax	(6.3)	(13.0)	(13.3)	(13.7)	(14.0)
<b>Total Revenues</b>	<b>(\$34.5)</b>	<b>(\$70.3)</b>	<b>(\$71.6)</b>	<b>(\$72.8)</b>	<b>(\$74.0)</b>

OTP: other tobacco product

Notes: Numbers may not sum to total due to rounding.

Source: Department of Legislative Services

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This estimate is based on (1) the estimated percentage of menthol and flavored cigarettes and OTPs consumed in the State in calendar 2015 and (2) available data on ESD sales in other states and in Montgomery County, adjusted for Maryland. It assumes that closed and cartridge-based ESDs comprise a significant percentage of ESD sales. In addition, it

assumes that most individuals who consume affected tobacco products will substitute other taxable products that are not affected by the bill and/or continue to consume menthol and flavored OTPs on-premises at smoking bars as permitted 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 2021. Future years reflect annualization and further declines in consumption.

To the extent that individuals do not substitute other taxable tobacco products or otherwise continue to consume menthol and flavored OTPs that are restricted to on-premises consumption, 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.

DLS advises there is considerable uncertainty about the impact recent FDA restrictions and recently announced enforcement action by the Comptroller's Office will have on the consumption of ESDs in the State 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 provisions 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 2021 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 penalties and expanded application of existing incarceration penalties 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.

ATC, once established, can likely 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 2021. 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 recent FDA and FED action on these products.

Local revenues (all counties) increase minimally as a result of the bill's monetary penalty provisions for unlawfully selling or shipping ESDs by mail or computer network for those cases heard in the circuit courts.

**Local Expenditures:** Expenditures increase as a result of the bill's incarceration penalties and expanded application of existing incarceration penalties. 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 tobacco products, including ESDs. However, sales may increase for small businesses that qualify as smoking bars to the extent that the bill's restrictions on the sale of flavored OTPs redirects the sales of such products to these establishments. Similarly, sales may increase for small business vape shops and other ESD retailers that primarily sell open ESDs to the extent that the bill's prohibition against the sale of closed and cartridge-based products increase sales of open ESDs permitted under the bill.

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 Comments:** It is assumed, for purposes of this fiscal and policy note, that "flavored tobacco product," as it appears in the bill, refers to a tobacco product that has a "characterizing flavor," as defined in the bill. Further, the bill inadvertently repeals the prohibition against distributing tobacco paraphernalia to an individual younger than age 21 (as part of the repeal of exceptions for active-duty military).

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## **Additional Information**

**Prior Introductions:** None.

**Designated Cross File:** SB 233 (The President, *et al.*) (By Request - Office of the Attorney General) - Finance.

**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

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