

Department of Legislative Services  
 Maryland General Assembly  
 2023 Session

FISCAL AND POLICY NOTE  
 First Reader

Senate Bill 259 (Senator Lam)  
 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 a significant but indeterminate amount beginning in FY 2023, as discussed below. General fund expenditures increase by \$531,000 in FY 2023 for one-time costs for the Maryland Department of Health (MDH) and personnel for the Alcohol and Tobacco Commission (ATC); future years reflect elimination of one-time costs and annualization. Also, general fund revenues and expenditures increase to the extent penalties are imposed, beginning in FY 2023 (not shown below).

(\$ in millions)	FY 2023	FY 2024	FY 2025	FY 2026	FY 2027
GF Revenue	(-)	(-)	(-)	(-)	(-)
GF Expenditure	\$0.5	\$1.0	\$1.1	\$1.1	\$1.2
Net Effect	(-)	(-)	(-)	(-)	(-)

*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 2023 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.

*Electronic Smoking Devices:* 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 or a battery or battery charger when sold separately.

## *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. ATC issues manufacturer, wholesaler, storage warehouse, and vending machine operator licenses. 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.

Federal legislation enacted in 2019 raised the minimum age for an individual to purchase or be sold tobacco products from 18 to 21.

## *Tobacco Product Taxes*

Chapter 37 of 2021 increased (1) the tobacco tax rate for cigarettes from \$2.00 to \$3.75 per pack of cigarettes and (2) the tobacco tax rate for OTP other than cigars and pipe tobacco from 30% to 53% of the wholesale price. Generally, the tax rate for cigars is 70% of the wholesale price. The tax rate for premium cigars is 15% of the wholesale price, and the tax rate for pipe tobacco is 30% of the wholesale price.

Chapters 767 and 768 of 2021 established licensure requirements for remote (out-of-state) tobacco sellers. Thus, effective July 1, 2022, a person located outside of the State must be a licensed remote tobacco seller in order to sell premium cigars and pipe tobacco to consumers in Maryland.

ESDs and their components are subject to the State sales and use tax but are not subject to a State excise tax. Chapter 37 increased the sales and use tax rate that generally applies to these products to 12% and increased the sales and use tax rate for vaping liquid sold in a container that contains up to 5 milliliters of vapid liquid to 60% of the taxable price. Montgomery County imposes a 30% tax on the wholesale value of vaping products.

**State Revenues:** Cigarette and OTP tax revenues accrue to the general fund. In fiscal 2022, cigarette tax revenues totaled \$417.9 million, and OTP tax revenues totaled \$55.6 million. In addition, the standard State sales and use tax rate of 6% is applied to the retail price of cigarettes and OTPs. A sales and use tax rate of 12% is imposed on the final retail price of ESDs (60% in the case of vaping liquid solid in a container that contains at least 5 milliliters of vaping liquid). Montgomery County imposes a 30% tax on the

wholesale value of vaping products. Montgomery County advises that the tax generated \$1.15 million in fiscal 2022 and estimates that revenues will total \$917,000 in fiscal 2023.

General fund revenues decrease significantly beginning in fiscal 2023 due to foregone tobacco excise tax and sales and use tax revenues under the bill's prohibition. The bill's *cumulative* effect on State revenues cannot be reliably determined at this time, as data on sales and use tax collections from the sale of ESDs and their components (which, as noted above, are subject to enhanced sales and use tax rates) are currently unavailable.

*For illustrative purposes only*, **Exhibit 1** shows the bill's estimated effect on tax revenues from the sale of *cigarettes and OTP* only. This estimate assumes the bill takes effect May 1, 2023; future years reflect a conservative reduction in cigarette and OTP tax revenues. In addition, this illustrative estimate assumes that most individuals who consume menthol and flavored 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 2024 and 2025.

Actual revenue losses under the bill are likely to be greater – by a potentially substantial amount – to the extent the bill reduces overall sales of ESDs and, thus, sales and use tax revenues from the sale of these products (not shown in the illustrative estimate below). Further, actual reductions in revenues from the sale of traditional tobacco products may be significantly greater than the illustrative estimate shown below to the extent that consumers do not substitute prohibited tobacco products for other taxable products. Also, to the extent the bill takes effect sooner than May 1, 2023, revenues losses in fiscal 2023 are greater.

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**Exhibit 1**  
**Illustrative Effects on Revenues from the Sale of Cigarettes and OTP**  
**Fiscal 2023-2027**  
**(\$ in Millions)**

	<u><b>FY 2023</b></u>	<u><b>FY 2024</b></u>	<u><b>FY 2025</b></u>	<u><b>FY 2026</b></u>	<u><b>FY 2027</b></u>
Cigarette Tax	(\$9.72)	(\$55.00)	(\$52.82)	(\$50.71)	(\$48.47)
OTP Tax	(2.79)	(16.24)	(16.84)	(17.55)	(18.23)
Sales and Use Tax	(2.78)	(15.71)	(15.60)	(15.49)	(15.00)
<b>Total Revenues</b>	<b>(\$15.29)</b>	<b>(\$86.95)</b>	<b>(\$85.25)</b>	<b>(\$83.75)</b>	<b>(\$81.70)</b>

OTP: other tobacco product

Notes: Numbers may not sum to total due to rounding. Fiscal 2023 revenue impacts reflect two months of impact only, assuming the bill takes effect May 1, 2023.

Source: Office of the Comptroller; Department of Legislative Services

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Finally, it is worth noting that in April 2022, FDA announced proposed product standards prohibiting menthol as a characterizing flavor in cigarettes and all characterizing flavors (other than tobacco) in cigars, with a proposed effective date of one year after publication of the final rule. The comment period closed on August 2, 2022. To the extent flavored products prohibited under the bill are ultimately prohibited via federal regulation, the potential revenue reductions discussed in this analysis may be observed in the absence of the bill. The Department of Legislative Services notes, however, that there is uncertainty regarding the timing of any federal regulatory action on these products. As of January 2023, FDA advises that it is committed to completing the rulemaking process in 2023.

**State Expenditures:**

*Maryland Department of Health*

General fund expenditures for MDH increase by an estimated \$66,300 in fiscal 2023 only for the department to update and supply training and educational materials for tobacco retailers and local health departments. Costs also reflect necessary mailings and modifications 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 that more people are committed to State correctional facilities for convictions in Baltimore City. Any such impact, however, is anticipated to be minimal.

*Alcohol and Tobacco Commission*

ATC general fund expenditures increase by at least \$464,665 in fiscal 2023 (assuming a start date of May 1, 2023). This estimate reflects the cost of hiring one agent supervisor and five agents for assessing and enforcing criminal and compliance regulations related to cigarettes, ESDs, and OTPs within the State. It includes salaries, fringe benefits, one-time start-up costs, contractual services, and ongoing operating expenses.

Positions	6.0
Salaries and Fringe Benefits	\$178,622
Contractual Services	1,564
One-time Start-up Costs	282,888
Other Operating Costs	<u>1,591</u>
<b>Minimum FY 2023 ATC Expenditures</b>	<b>\$464,665</b>

Future year expenditures reflect full salaries with annual increases and employee turnover as well as annual increases in ongoing operating expenses. In addition, the estimate includes ongoing contractual costs for services related to the destruction of evidence collected by agents.

**Local Revenues:** As noted above, Montgomery County imposes a 30% tax on the wholesale value of vaping products, which generated \$1.15 million in fiscal 2022 and is estimated to generate \$917,000 in fiscal 2023. Under the bill, Montgomery County tax revenues decline beginning in fiscal 2023. The amount of the decline depends on the decrease in vaping products sold as a result of the bill.

**Local Expenditures:** Expenditures increase minimally as a result of the bill's incarceration penalty. Counties pay the full cost of incarceration for people in their facilities for the first 12 months of the sentence. A \$45 per diem State grant is provided to each county for each day between 12 and 18 months that a sentenced inmate is confined in a local detention center. Counties also receive an additional \$45 per day grant for inmates who have been sentenced to the custody of the State but are confined in or who receive reentry or other prerelease programming and services from a local facility. Per diem operating costs of local detention facilities have ranged from approximately \$90 to \$300 per inmate in recent years.

**Small Business Effect:** Sales decline, significantly in some cases, for small businesses in Maryland that sell flavored tobacco products. ATC advises there are approximately 6,000 retail licenses in the State. A vast majority of these businesses are small convenience stores that offer flavored tobacco products for sale. Flavored tobacco product sales represent a significant portion of their revenues, prohibiting such sales likely leads to a reduction in revenue for these businesses. Moreover, with an immediate effective date, the

bill does not allow for the sale of any product already in stock that is prohibited under the bill.

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### **Additional Information**

**Prior Introductions:** Similar legislation has been introduced within the last three years. See SB 233 of 2022.

**Designated Cross File:** None.

**Information Source(s):** Maryland Association of County Health Officers; Montgomery County; Alcohol and Tobacco Commission; Comptroller's Office; Judiciary (Administrative Office of the Courts); Maryland Department of Health; Department of Legislative Services

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