

MINNESOTA • REVENUE

MNCare, Cigarette, and Tobacco Taxes Rate Changes and Dedication

April 11, 2003

	Yes	No
Separate Official Fiscal Note Requested		
Fiscal Impact		
DOR Administrative Costs/Savings		

Department of Revenue

Analysis of H.F. 29 (Bradley) - Revised for 1st Engrossment and February 2003 Forecast

	Revenue Gain or (Loss)			
	<u>F.Y. 2004</u>	<u>F.Y. 2005</u>	<u>F.Y. 2006</u>	<u>F.Y. 2007</u>
	(000's)			
Cigarette Excise Tax	(\$23,512)	(\$24,271)	(\$23,023)	(\$21,835)
Cigarette Tax Refunds	(\$5,492)	(\$6,083)	(\$6,166)	(\$6,245)
Sales Tax on Cigarettes	\$6,442	\$7,184	\$7,320	\$7,447
Tobacco Excise Tax	(\$4,619)	(\$5,215)	(\$5,398)	(\$5,587)
Sales Tax on Tobacco Products	<u>\$434</u>	<u>\$490</u>	<u>\$507</u>	<u>\$525</u>
General Fund Total	(\$26,747)	(\$27,895)	(\$26,760)	(\$25,695)
Cigarette Excise Tax	\$266,411	\$291,893	\$292,885	\$293,753
Tobacco Excise Tax	\$26,472	\$29,889	\$30,935	\$32,017
Cigarette Floor Stocks Tax	\$25,000	\$0	\$0	\$0
Tobacco Floor Stocks Tax	\$5,000	\$0	\$0	\$0
MNCare Tax Repeal	(\$196,113)	(\$317,156)	(\$348,494)	(\$381,211)
Health Care Access Fund Total	\$126,770	\$4,626	(\$24,674)	(\$55,441)
Minnesota Future Resources Fund	<u>(\$1,022)</u>	<u>(\$1,055)</u>	<u>(\$1,001)</u>	<u>(\$949)</u>
Total All Funds	\$99,001	(\$24,324)	(\$52,435)	(\$82,085)

Effective July 1, 2003

EXPLANATION OF THE BILL

Current Law: A gross revenue tax (MinnesotaCare Tax) of 1.5% is imposed on hospitals, health care providers, surgical centers, and wholesale drug distributors. Revenues are deposited in the Health Care Access Fund. Beginning January 1, 2004, the tax rate will be 2%.

The cigarette tax rate is 48¢ per pack of 20 cigarettes. The Minnesota Future Resources Fund receives 2¢ from every pack. The balance of the cigarette tax revenue is deposited in the General Fund. The tobacco products tax rate is 35% of the wholesale price. All revenues from the tobacco products tax are deposited in the General Fund.

EXPLANATION OF THE BILL (cont.)

Cigarette distributors receive a discount of 1.0% of face value for the first \$1,500,000 of annual stamp purchases and 0.6% of the amount over \$1,500,000. Distributors of tobacco products receive a discount equal to 1.5% of the tax.

Proposed Law: As amended, the bill would repeal the MinnesotaCare taxes, effective for gross revenues received by the taxpayer after June 30, 2003, and replace these revenues with dedicated increases in the cigarette and the tobacco product taxes. A floor stocks tax is also imposed on cigarettes and tobacco products.

The proposal is to raise the cigarette tax rate from 48¢ to \$1.48 per pack of 20. The Minnesota Future Resources Fund will continue to receive 2¢ per pack, and 46¢ per pack will continue to be credited to the General Fund. The proposal would raise the tobacco products tax rate from 35% to 108% of wholesale price, and 35% of the wholesale price of tobacco products would continue to be credited to the general fund. The proposal would impose a floor stocks tax (i.e. a tax on current inventories) on cigarettes and also one on tobacco products. Revenues from the increases in the taxes are to be deposited in the Health Care Access Fund.

The discount for cigarette distributors would change from 1.0% to 0.32% of face value for the first \$1,500,000 of annual stamp purchases and from 0.6% to 0.19% of the excess. The discount for tobacco products distributors would be decreased from 1.5% to 0.49%.

REVENUE ANALYSIS DETAIL

MinnesotaCare Taxes:

- Baseline revenues from the February 2003 forecast were used for the various tax categories.
- Because the proposal is effective for gross revenues received after June 30, 2003, the impact in fiscal year 2004 reflects eleven months of estimated tax payments for hospitals and surgical centers, three quarterly payments of estimated tax for health care providers and wholesale drug distributors, and an adjustment for refunds for tax year 2003.

Cigarette and Tobacco Taxes:

- Baseline revenues are the February 2003 forecast for the cigarette and tobacco taxes.
- An elasticity factor of -0.55 was applied for changes in consumption due to the tax increase. As such, General Fund and Minnesota Future Resources Fund revenues under the proposal decline due to reduced consumption.
- The average retail price of cigarettes is predicted to grow at an annual rate of 5%.

REVENUE ANALYSIS DETAIL (cont.)

- Indian cigarette and tobacco tax refunds grow at a proportional rate to the tax increase. All refunds would continue to be paid from the general fund.
- Because this law becomes effective July 1, 2003, 11 months of collections would be realized in fiscal year 2004.
- It was estimated that approximately 25 million packs of cigarettes would be subject to the floor stocks tax.
- The floor stocks tax for tobacco products is estimated to be 10% of the cigarette floor stocks revenue when the relative size of the retail cigarette prices and the tobacco products retail price changes are similar. A factor for the relatively larger size of the tobacco products retail price change for this proposal is included in the estimate of the tobacco products floor stocks tax.

NUMBER OF TAXPAYERS AFFECTED: 75 distributors for cigarettes and 180 distributors for tobacco products. 6,770 health care providers, 150 hospitals/surgical centers, and 140 wholesale drug distributors.

Source: Minnesota Department of Revenue

Tax Research Division

<http://www.taxes.state.mn.us/polic.html#analyses>