

MINNESOTA • REVENUE

MNCare, Cigarette, Tobacco Taxes Rate and Disposition Changes

April 2, 2004

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

Department of Revenue
Analysis of S.F. 2602 (Lourey) / H.F. 2870 (Huntley) – Tax Provisions Only

	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	\$0	\$106,675	\$117,283	\$118,069
Cigarette Tax Refunds	\$0	(\$5,613)	(\$6,207)	(\$6,287)
Sales Tax on Cigarettes	\$0	\$6,411	\$7,091	\$7,178
Tobacco Excise Tax	\$0	(\$7,377)	(\$8,340)	(\$8,631)
Sales Tax on Tobacco Products	\$0	\$549	\$621	\$643
Appropriation to MN Comprehensive Health Assoc.	\$0	(\$50,000)	(\$50,000)	(\$50,000)
Appropriation for Tobacco Prevention	\$0	(\$5,000)	\$0	\$0
Appropriation for Children w/Special Needs	<u>\$0</u>	<u>(\$1,500)</u>	<u>(\$1,500)</u>	<u>(\$1,500)</u>
General Fund Total*	\$0	\$44,145	\$58,948	\$59,472
MNCare Tax Reduction	(\$27,480)	(\$87,900)	(\$95,030)	(\$103,520)
Cigarette Excise Tax	\$0	\$135,460	\$147,542	\$147,238
Tobacco Excise Tax	\$0	\$32,225	\$36,432	\$37,699
Cigarette Floor Stocks Tax	<u>\$0</u>	<u>\$28,000</u>	<u>\$0</u>	<u>\$0</u>
Health Care Access Fund Total	(\$27,480)	\$107,785	\$88,944	\$81,417
Academic Health Center Fund	\$0	(\$3,061)	(\$3,151)	(\$2,974)
Medical Education & Research Account, Special Revenue Fund	<u>\$0</u>	<u>(\$1,177)</u>	<u>(\$1,213)</u>	<u>(\$1,144)</u>
Total All Funds	(\$27,480)	\$147,692	\$143,528	\$136,771

* In addition to the amounts shown, the bill includes unspecified appropriations from the general fund.

The MinnesotaCare changes are effective for gross revenues received on or after January 1, 2004.
The cigarette and tobacco tax changes are effective July 1, 2004.

EXPLANATION OF THE BILL

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

The cigarette tax rate is 48¢ per pack of 20 cigarettes. The Academic Health Center fund receives 6.5¢ per pack and the Medical Education and Research Account in the Special Revenue Fund receives 2.5¢ per pack. The balance of the cigarette tax revenue (39¢ per pack) 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.

Proposed Law: The bill would reduce the MinnesotaCare tax rate from 2.0% to 1.5%. The proposal to reduce the tax rate effective retroactively would require some adjustment for estimated taxes already paid. For calendar years 2005 and after, the rate for each year would depend upon the balance in the Health Care Access Fund. If a structural deficit is projected, the rate for that year would be 2%.

The proposal would raise the cigarette tax rate from \$0.48 to \$1.48 per pack of 20. The \$1.48 would be distributed to four funds. The amount to the general fund would be increased from 39¢ per pack to 87¢ per pack. The amounts due to the Academic Health Center Fund and the Medical Education and Research Account of the Special Revenue Fund would continue to be 6.5¢ and 2.5¢ per pack. The balance of 52¢ per pack would be deposited in the Health Care Access Fund.

The proposal would impose a floor stocks tax (i.e. a tax on current inventories) on cigarettes. The floor stocks tax is imposed on persons engaged in selling cigarettes (on all cigarette stamps) at a rate of \$1.00 per pack. The cigarette floor stocks tax is to be applied on all cigarette stamps in the inventory of the sellers as of July 1, 2004. Revenues from the floor stocks taxes are to be deposited in the Health Care Access Fund.

The proposal would raise the tobacco products tax rate from 35% to 108% of wholesale price. Revenues from the tobacco tax would be distributed 27% to the General Fund and 73% to the Health Care Access Fund.

Seven appropriations are provided by the proposal, six from the General Fund and one from the Health Care Access Fund. Three of the appropriations have amounts specified in the bill language, and four of the appropriations are left blank.

Appropriations of specific amounts are made from the General Fund: 1) \$50 million to the Minnesota Comprehensive Health Association to offset assessments (also for FY2006 and FY2007), 2) \$1.5 million to the Commissioner of Health for the children with special health care needs program (also for FY2006 and FY2007), and 3) \$5 million to the Commissioner of Health for grant awards for fiscal year 2005.

EXPLANATION OF THE BILL (cont.)

Appropriations of an unspecified amount are made from the General Fund to: 1) the Commissioner of Human Services to pay the state matching amount for the increased disproportionate share hospital payments under the 2003 Medicare Act, 2) the Commissioner of Human Services for reimbursements to critical access dental providers (also for FY2006 and FY2007), and 3) the Commissioner of Human Services for implementing the proposal. Another appropriation of an unspecified amount is made from the Health Care Access Fund to the Commissioner of Human Services for implementing the proposal.

REVENUE ANALYSIS DETAIL

MinnesotaCare Taxes:

- Baseline revenues from the February 2004 forecast were used.
- Because the proposal is effective for gross revenues received on or after January 1, 2004, the impact in fiscal year 2004 reflects five months of estimated tax payments for hospitals and surgical centers and one quarterly payment of estimated tax for health care providers and wholesale drug distributors.
- It is assumed that the rate would remain at 1.5% for the forecast period and would not be increased due to a projected structural deficit in the Health Care Access Fund.

Cigarette and Tobacco Taxes:

- Baseline revenues are the February 2004 forecast for the cigarette and tobacco taxes.
- An elasticity factor of -0.55 was applied for changes in consumption due to the cigarette and tobacco tax increases.
- The average retail price of cigarettes is predicted to grow at an annual rate of 5%.
- 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, 2004, 11 months of collections would be realized in fiscal year 2005.
- It is assumed that the fund distributions for cigarettes are to be calculated as the gross revenue times the tax rate increase compared to the tax total (i.e. \$0.87 / \$1.48, \$0.52 / \$1.48, \$0.065 / \$1.48, and \$0.025 / \$1.48). Similarly, it is assumed that the tobacco increase is 27% of the revised total excise tax revenue amount.
- It is estimated that approximately 28 million packs of cigarettes would be subject to the \$1.00 per pack 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/taxes/legal_policy