

MINNESOTA • REVENUE

CIGARETTE EXCISE TAX AND FEE TOBACCO PRODUCTS TAX AND FEE Little Cigars Classified as Cigarettes

March 26, 2013

House Companion Bill Added

	Yes	No
DOR Administrative Costs/Savings	X	

Department of Revenue
Analysis of S.F. 135 (Nelson) / H.F. 1619 (Loon)

	Fund Impact			
	<u>F.Y. 2014</u>	<u>F.Y. 2015</u>	<u>F.Y. 2016</u>	<u>F.Y. 2017</u>
	(000's)			
Cigarette Excise Tax	\$2,500	\$2,700	\$2,700	\$2,700
Tobacco Products Excise Tax	(\$1,900)	(\$2,100)	(\$2,100)	(\$2,100)
Sales Tax on Cigarettes	\$1,500	\$1,700	\$1,700	\$1,700
Sales Tax on Tobacco Products	(\$800)	(\$800)	(\$800)	(\$800)
Cigarette Non-Settlement Fee	<u>\$1,400</u>	<u>\$1,500</u>	<u>\$1,500</u>	<u>\$1,500</u>
General Fund Net Total*	\$2,700	\$3,000	\$3,000	\$3,000
Cigarette Health Impact Fee	\$4,000	\$4,300	\$4,200	\$4,200
Tobacco Products Health Impact Fee	<u>(\$1,900)</u>	<u>(\$2,100)</u>	<u>(\$2,100)</u>	<u>(\$2,100)</u>
Health Impact Fund Net Total	\$2,100	\$2,200	\$2,100	\$2,100
Natural Resources and Arts Funds	(\$40)	(\$50)	(\$50)	(\$50)
Total – All Funds	\$4,760	\$5,150	\$5,050	\$5,050

*The FY 2014 impact would also include an appropriation for the cost of the report, which is left blank in the bill.

Assumed to be effective July 1, 2013.

EXPLANATION OF THE BILL

Current Law: The definition of cigarettes is any roll for smoking made wholly or in part of tobacco, the wrapper or cover of which is made of paper or another substance or material, except tobacco. Cigarettes are taxed on a per pack basis – the cigarette excise tax of 48¢ per pack, the cigarette health impact fee of 75¢ per pack, the cigarette in-lieu sales tax (36.2¢ in calendar year 2013), and the cigarette non-settlement fee of 35¢ per pack. Cigarettes weighing more than three pounds per thousand have a cigarette excise tax of 96¢ per pack, cigarette health impact fee of \$1.50 per pack, the in-lieu sales tax, and the 35¢ per pack non-settlement fee.

The definition of tobacco products specifically includes a variety of tobacco items including little cigars. Tobacco products other than cigarettes are subject to the tobacco products excise tax of 35% of the wholesale price and the tobacco products health impact fee of 35% of the wholesale price.

Proposed Law: The bill expands the definition of cigarettes to include any roll for smoking made wholly or in part of tobacco weighing 4.5 pounds or less per thousand and changes the wrapper definition to include items wrapped in any substance containing tobacco which, because of the appearance, size, packaging, pricing, marketing, or labeling is likely to be offered to or purchased by consumers as a cigarette.

EXPLANATION OF THE BILL (Cont.)

The primary effect of the wording changes is to tax little cigars as cigarettes. The tobacco products excise tax and fee of 70% of the wholesale price and the sales and use tax on other tobacco products would be replaced with individual pack charges currently placed on cigarettes.

The bill requires that the Commissioner of Revenue report to the 2014 Legislature on the tobacco tax collection system. The report is to provide information and guidance to the Legislature on possible improvements to the tobacco tax collection system, including recommendations that will increase compliance. A general fund appropriation of an unspecified amount is provided for the cost of the report.

REVENUE ANALYSIS DETAIL

- The November 2012 forecast amounts are used.
- For fiscal year 2014, sales of 226,700,000 packs of cigarettes are estimated under current law.
- Little cigar production is estimated to be 3% of cigarette production based on national data.
- Wholesale brand, price, and market share information is based on wholesale distributor data provided by the Minnesota Department of Revenue – Special Taxes Division. Information from sixteen little cigar brands were aggregated to determine the estimates for price and market share.
- The average wholesale price of little cigars is assumed to be 85¢ per pack in fiscal year 2014.
- Little cigar prices are assumed to grow at 2% annually (consistent with cigarette price growth).
- Little cigars are currently being produced at a weight of over three pounds per thousand and are subject to a federal excise tax at the large cigar rate of 52.75% of the sales price. For little cigars that are three pounds per thousand or less, the federal tax rate is \$1.01 per pack (equal to the federal cigarette rate). It is assumed that the industry would continue to sell little cigars that are over three pounds per thousand so the federal tax rate is 52.75% and the state excise rates are 96¢ tax and \$1.50 fee.
- The proposal would increase the price per pack of little cigars to be closer to the average price per pack of cigarettes. The significant increase in product price limits use of elasticity factors.
- It is assumed that the little cigar market would be reduced to 20% of the current market, 45% of the market would substitute cigarettes for little cigars, and 35% of the little cigar retail market would be lost due to consumption reductions.
- It is assumed that little cigars would be subject to the 35¢ per pack non-settlement fee.
- The impact of the changes on cigarette and tobacco tax refunds is minimal.
- No adjustment is made for market behavior prior to the implementation date of July 1, 2013.
- Fiscal year 2014 is adjusted for 11 months of collections.

Number of Taxpayers: There are approximately 175 wholesalers of other tobacco products and 50 wholesalers of cigarettes in Minnesota. Also, there are about 9,000 retailers of tobacco products.

Source: Minnesota Department of Revenue
Tax Research Division
http://www.revenue.state.mn.us/research_stats/Pages/Revenue-Analyses.aspx