

STORAGE NAME: h0991c.ft

DATE: April 9, 1999

**HOUSE OF REPRESENTATIVES
AS REVISED BY THE COMMITTEE ON
FINANCE AND TAXATION
ANALYSIS**

BILL #: HB 991

RELATING TO: Tax on tobacco products; creating a primary source of supply

SPONSOR(S): Representative(s) Albright; Andrews and others

COMPANION BILL(S): SB 2248 (Identical)

ORIGINATING COMMITTEE(S)/COMMITTEE(S) OF REFERENCE:

- (1) GOVERNMENTAL RULES AND REGULATIONS YEAS 7 NAYS 0
 - (2) FINANCE AND TAXATION YEAS 13 NAYS 0
 - (3) GENERAL GOVERNMENT APPROPRIATIONS
 - (4)
 - (5)
-

I. SUMMARY:

The bill requires domestic cigarette manufacturers to register as the primary source of supply prior to offering their cigarettes for sale in the state. In the case of cigarettes manufactured outside of the United States, the primary source of supply may be the manufacturer or may be an agent of the manufacturer. Wholesale dealers in Florida will be prohibited from purchasing cigarettes from anyone other than the primary source of supply.

The bill requires that prior to issuance of a temporary cigarette permit, final approval of a cigarette permit, and prior to annual renewal of a cigarette permit, the applicant must provide the Division of Alcoholic Beverages and Tobacco with an affirmation from the manufacturer, or in the case of cigarettes manufactured outside of the United States from the primary source of supply, that the manufacturer intends to provide cigarettes to the applicant.

The bill provides penalties for non-compliance and makes various technical amendments to Chapter 210.

The bill may result in an indeterminate increase in cigarette tax collections. The cost to the division of implementing this legislation is insignificant.

The act would take effect upon becoming a law.

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II. SUBSTANTIVE ANALYSIS:

A. PRESENT SITUATION:

Chapter 210, F.S., provides the regulatory and tax structure for Florida's tobacco laws. The Division of Alcoholic Beverages and Tobacco of the Department of Business and Professional Regulation is charged with supervising the distribution of cigarettes and other tobacco products including: issuing permits for cigarette distributing agents, wholesale dealers, exporters, and retail dealers; collection and deposit of related taxes and fees; conducting audits; making tax assessments; seizing non-tax paid products; conducting criminal and administrative investigations; and imposing penalties for violations. Part I of Chapter 210 addresses cigarettes and Part II addresses other tobacco products [OTP].

Cigarettes are a highly taxed and highly regulated product in the State of Florida. Florida has one of the highest excise tax rates on cigarettes in the nation. For FY 1997/98 cigarette excise taxes generated over \$449.5 million in revenue for the state.

Section 210.15, F.S., requires every person or business desiring to deal in cigarettes as a distributing agent, wholesale dealer, or exporter to obtain a cigarette permit and establishes standards for qualification. Temporary permits are issued upon payment of the applicable fee and filing of a completed application which, on its face, does not disclose any impairment to licensure.

The permit fee for a distributing agent is statutorily established at \$5 and is reissued annually upon payment of the \$5 fee. Distributing agents receive cigarettes in interstate or intrastate commerce and typically warehouse the cigarettes while awaiting distribution instructions from the manufacturer. Distributing agents, at the direction of the manufacturer, then distribute the cigarettes to wholesale dealers or to other distributing agents.

Wholesale dealers are defined as persons or businesses who sell cigarettes to retailers or to other wholesalers. The annual permit fee for a wholesale dealer is statutorily set at \$100 and is reissued annually upon payment of the \$100 fee. Anyone who operates more than one cigarette vending machine in more than one location is also classified as a wholesale dealer.

Wholesale dealers may be either "stamping agents" or non-stamping "tax-paid" wholesalers. A stamping agent wholesaler pays the state cigarette excise tax required by s. 210.02, F.S., at the time the agent obtains the cigarette tax stamps from the division or the stamping agent may arrange credit terms. These stamping agents place the excise tax stamps on cigarette packages prior to resale to other wholesalers or retailers. The division regulates approximately 120 cigarette stamping agent wholesalers. Tax-paid wholesale dealers receive cigarettes from stamping agents with the tax stamps already affixed. The division regulates approximately 400 non-stampers. Compared to last year, the number of licensed cigarette wholesale dealers is down by 19 percent or 100 dealers.

Exporters receive or transport tax-exempt cigarettes for delivery beyond the borders of the state and store them in bonded warehouses prior to shipment into foreign commerce. The annual permit fee for exporters is statutorily set at \$100 and is reissued annually upon payment of the \$100 fee.

There is no statutory definition for a cigarette importer. Importers, or persons who obtain cigarettes via foreign commerce, are licensed as wholesale dealers. These wholesalers typically receive cigarettes which have been shipped by the international arm of a domestic cigarette manufacturer to a foreign country but are diverted from that destination for various reasons. A consumption entry document for returned American goods is filed by the importer with the federal government at which time federal excise taxes are paid on the cigarettes. When the cigarettes clear U. S. Customs, they are moved from a bonded warehouse to a non-bonded facility. At that point, the wholesaler/importer is required to affix the Florida excise tax stamp to the product prior to its further distribution. The division has limited ability to monitor the movement of cigarettes through customs since the location is outside the state's jurisdiction.

Wholesale dealers who import cigarettes from the foreign commerce stream are usually able to purchase the cigarettes at a cost substantially less than those wholesale dealers who purchase the product through the domestic market.

Recent amendments to the Internal Revenue Code will prohibit, effective January 1, 2000, the release from customs custody of previously exported cigarettes to anyone other than a cigarette manufacturer or to a bonded export warehouse. [Pub.L. 105-33, Title IX, 111 Stat. 673.]

B. EFFECT OF PROPOSED CHANGES:

The bill creates a regulatory structure, similar to that in existence for the regulation of wine and liquor, which prohibits a wholesale dealer from purchasing cigarettes from anyone other than the "primary source of supply." Each domestic manufacturer, whose brand is sold in Florida, must register with the Division of Alcoholic Beverages and Tobacco (DABT/division) as the primary source of supply. In the case of cigarettes manufactured outside of the United States, the primary source of supply may be an agent of the manufacturer, who, if the brand cannot be secured directly from the manufacturer by a wholesale dealer, is the source closest to the foreign manufacturer in the channel of commerce from whom the brand can be secured by an American permit holder.

Likewise, the bill prohibits the shipment from another state or a foreign country into this state, except directly by the registered primary source of supply. This provision would not prohibit another distributing agent or a wholesale dealer from receiving cigarettes from a distributing agent since the distributing agent acts as an arm of the manufacturer for distribution purposes.

In order to assist in tracking the movement of all cigarettes, the primary source of supply is required to provide the division a listing of their complete product line and a report of all shipments into the state. This information must be updated monthly. The DABT estimates that there are presently over 100 different brands of cigarettes, each having between 5 and 20 extensions, i.e., lights, menthol, etc.

The bill prohibits the application of labels, decals, etc. to any package of cigarettes unless done so in accordance with the Federal Cigarette Labeling and Advertising Act. Moreover, the bill prohibits the placement of a tax stamp on any cigarette package that contains any notice or label identifying the cigarettes as intended for use outside of the United States or exempt from federal taxes.

The bill requires that prior to issuance of a temporary initial cigarette permit or final approval of a cigarette permit, the applicant must file an affirmation from the manufacturer which attests to the manufacturer's intent to provide cigarettes to the applicant. In the case of cigarettes manufactured outside of the United States, the affirmation may be received from the registered primary source of supply. A newly executed affirmation must be filed annually as a condition of permit renewal.

Combined, these provisions will preclude a wholesale dealer from importing cigarettes, which were originally destined for a foreign market, into Florida. Moreover, the bill creates a regulatory mechanism which provides the division with increased capability to track the movement of this taxable product from the manufacturer to the ultimate consumer. Cigarettes found in the possession of a wholesaler or retailer in violation of this requirement are subject to seizure and forfeiture. The division is also authorized to administratively fine, suspend, or revoke the permit of a wholesale dealer or the registration of a primary source of supply for violations of the law.

The bill amends the fingerprint requirements in Chapter 210 to make the requirement for submission of fingerprints permissive upon the request of the division rather than mandatory and makes other technical amendments to the cigarette permitting statute.

The requirements set forth in this legislation apply only to the commerce of cigarettes and not to other tobacco products such as snuff, cigars, etc.

C. APPLICATION OF PRINCIPLES:

1. Less Government:

- a. Does the bill create, increase or reduce, either directly or indirectly:

(1) any authority to make rules or adjudicate disputes?

Yes. The bill authorizes the division to establish permit renewal dates by rule.

(2) any new responsibilities, obligations or work for other governmental or private organizations or individuals?

N/A

(3) any entitlement to a government service or benefit?

N/A

b. If an agency or program is eliminated or reduced:

(1) what responsibilities, costs and powers are passed on to another program, agency, level of government, or private entity?

N/A

(2) what is the cost of such responsibility at the new level/agency?

N/A

(3) how is the new agency accountable to the people governed?

N/A

2. Lower Taxes:

a. Does the bill increase anyone's taxes?

N/A

b. Does the bill require or authorize an increase in any fees?

N/A

c. Does the bill reduce total taxes, both rates and revenues?

N/A

d. Does the bill reduce total fees, both rates and revenues?

N/A

e. Does the bill authorize any fee or tax increase by any local government?

N/A

3. Personal Responsibility:

a. Does the bill reduce or eliminate an entitlement to government services or subsidy?

N/A

- b. Do the beneficiaries of the legislation directly pay any portion of the cost of implementation and operation?

N/A

4. Individual Freedom:

- a. Does the bill increase the allowable options of individuals or private organizations/associations to conduct their own affairs?

N/A

- b. Does the bill prohibit, or create new government interference with, any presently lawful activity?

Yes. At present wholesale dealers may import domestically manufactured cigarettes which were packaged and destined for a foreign market into the state, pay the applicable state and federal excise taxes, and distribute to retail dealers. The provisions of the bill will effectively prevent the continuation of this practice.

5. Family Empowerment:

- a. If the bill purports to provide services to families or children:

- (1) Who evaluates the family's needs?

N/A

- (2) Who makes the decisions?

N/A

- (3) Are private alternatives permitted?

N/A

- (4) Are families required to participate in a program?

N/A

- (5) Are families penalized for not participating in a program?

N/A

- b. Does the bill directly affect the legal rights and obligations between family members?

N/A

- c. If the bill creates or changes a program providing services to families or children, in which of the following does the bill vest control of the program, either through direct participation or appointment authority:

- (1) parents and guardians?

N/A

(2) service providers?

N/A

(3) government employees/agencies?

N/A

D. STATUTE(S) AFFECTED:

Sections 210.155, 210.15, 210.151, 210.16 and 210.405, Florida Statutes.

E. SECTION-BY-SECTION ANALYSIS:

Section 1. Creates s. 210.155, F.S., to provide that in the case of domestic cigarettes, each cigarette manufacturer must register as the primary source of supply for all of that manufacturer's cigarette brands which are offered for sale in the state. A foreign cigarette manufacturer or an agent of a foreign cigarette manufacturer may be registered as the primary source of supply. No cigarette product shall be shipped into Florida from another state or foreign country except from the primary source of supply, registered as required in subsection (2), for the brand of cigarettes being shipped. Packages sold within this state having an affixed or imprinted stamp, decal, or other cover must comply with all requirements of the Federal Cigarette Labeling and Advertising Act. Cigarettes found in the state in violation of this section are subject to seizure and forfeiture.

Section 2. Amends s. 210.15, F.S., to require that each cigarette wholesale dealer permit application be accompanied by an affirmation from the manufacturer on a form approved by the division. This affirmation must confirm the manufacturer's intent to provide cigarettes to the distributing agent or wholesale dealer who is applying for the permit and must be received by the division prior to final approval of the permit. In the case of cigarettes manufactured outside of the United States, the permit application must be accompanied by an affirmation from the primary source of supply, which may be the manufacturer or may be an agent of the manufacturer. Under all circumstances, a newly executed affirmation must be filed annually with the division as a condition of permit renewal. This section also makes submission of fingerprints by applicants for licensure dependent upon the division's request for same and makes other technical changes.

Section 3. Amends s. 210.151, F.S., to specify that the manufacturer's affirmation required by s. 210.15, F.S., must be received by the division prior to issuance of a temporary initial cigarette permit. Amends language concerning expiration of temporary permits and deletes references to other tobacco products.

Section 4. Amends s. 210.405, F.S., to delete references to initial temporary cigarette permits and amends language concerning the expiration of temporary tobacco products permits.

Section 5. Amends s. 210.16, F.S., to grant power and authority to the division to administratively fine, suspend, or revoke the registration of a primary source of supply. Provides that no primary source of supply registration can be renewed for six months after a revocation becomes final. Increases the limitation on civil penalties from \$1,000 to \$100,000.

Section 6. Provides that the act shall take effect upon becoming a law.

III. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT:

A. FISCAL IMPACT ON STATE AGENCIES/STATE FUNDS:

1. Non-recurring Effects:

The division will incur the initial cost of establishing this registration process, i.e., printing, notification, etc.

2. Recurring Effects:

Revenues: See section D., Fiscal Comments.

Expenditures: The division will incur the ongoing cost associated with registrations as the primary source of supply which are required by this bill.

3. Long Run Effects Other Than Normal Growth:

N/A

4. Total Revenues and Expenditures:

See A.1. and A.2. above.

B. FISCAL IMPACT ON LOCAL GOVERNMENTS AS A WHOLE:

1. Non-recurring Effects:

N/A

2. Recurring Effects:

Revenues: See section D., Fiscal Comments.

3. Long Run Effects Other Than Normal Growth:

If the enhanced audit capabilities provided by this legislation results in the collection of increased excise tax revenue, local governments will benefit to the degree the various trust funds receive allocations.

C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

1. Direct Private Sector Costs:

Cigarette retailers purchasing cigarettes at a reduced cost from wholesalers who obtain products diverted from the international market, will experience an increase in the cost of the product. Likewise, if these retailers passed their cost savings on to the ultimate consumer, and are now unable to do so, the consumer will experience an increase in the cost of the product.

Some wholesalers who only deal in previously exported cigarettes may cease operation since the financial advantage for purchasing exported cigarettes versus purchasing cigarettes through domestic channels will be eliminated.

2. Direct Private Sector Benefits:

N/A

3. Effects on Competition, Private Enterprise and Employment Markets:

Proponents of this legislation believe this regulatory structure equalizes competition by ensuring that cigarette wholesalers in Florida, who obtain their products from traditional domestic sources, do not operate at a competitive disadvantage with wholesalers who may obtain cigarettes at a reduced price via the international market.

D. FISCAL COMMENTS:

The provisions of this bill will assist the division in tracking the movement of cigarettes in the state and may result in an indeterminate increase in collection of cigarette excise tax revenue. Such increase in tax revenue would be distributed to the following funds in accordance with the percentages specified in s. 212.20, F.S.: General Revenue Fund, Alcoholic Beverage and Tobacco Trust Fund, Public Medical Assistance Trust Fund, Municipal Financial Assistance Trust Fund, and the Revenue Sharing Trust Funds for Municipalities and Counties.

IV. CONSEQUENCES OF ARTICLE VII, SECTION 18 OF THE FLORIDA CONSTITUTION:

A. APPLICABILITY OF THE MANDATES PROVISION:

The bill does not require the counties or municipalities to spend funds or to take an action requiring the expenditure of funds.

B. REDUCTION OF REVENUE RAISING AUTHORITY:

The bill does not reduce the authority that municipalities or counties have to raise revenue in the aggregate.

C. REDUCTION OF STATE TAX SHARED WITH COUNTIES AND MUNICIPALITIES:

The bill does not reduce the percentage of a state tax shared with counties or municipalities.

V. COMMENTS:

The following are comments by the Committee on Governmental Rules and Regulations on March 17, 1999:

This regulatory structure was generally patterned after those already in place for the registration of wine and spirits. To cover the cost of registration, the primary source of supply is required to pay a brand registration fee for each brand of wine or spirits registered with the division. There is no similar provision in this bill to cover the cost of registration for the different brands of cigarettes.

An issue addressed by Representative Albright relates to the loss of revenues in the tobacco settlement because of the lost count of cigarettes sold in Florida under the gray market. The monetary loss to the State of Florida is estimated at \$5 to \$7 million per year, although representatives of the Florida Tobacco and Candy Association estimate a loss of \$20 million per year.

The provisions of the bill are currently provisions found in a federal law passed to address gray markets. Even if the bill does not pass the House and Senate, the provision of the bill will still be in effect due to the federal legislation.

VI. AMENDMENTS OR COMMITTEE SUBSTITUTE CHANGES:

The House Committee on Governmental Rules and Regulations considered this bill on March 8, 1999, and adopted the following amendments:

Amendment 1. This is a technical amendment recommended by staff to conform the bill to current practice in identifying grants of rulemaking authority.

Amendment 2. This is a technical amendment recommended by staff to conform the bill to current practice in identifying grants of rulemaking authority.

Amendment 3. This is a technical amendment recommended by staff to conform the bill to current practice in identifying grants of rulemaking authority.

Amendment 4. This is a technical amendment recommended by staff to conform the bill to current practice in identifying grants of rulemaking authority.

The House Committee on Governmental Rules and Regulations considered this bill on March 17, 1999, and adopted amendment five:

Amendment 5. This amendment changes the effective date of the bill to January 1, 2000. Originally, the bill's effective date commenced upon signing into law. The amendment conforms HB 991 with existing federal legislation that requires an effective date of January 1, 2000. The federal legislation implements similar provisions.

The House Finance and Taxation Committee adopted a "strike-all" amendment that made the following changes:

- permits cigarettes designated for export to be redirected to a bonded warehouse or manufacturer pursuant to federal regulations.
- permits a holder of interim wholesale dealer permits to affix stamps and decals to non-compliant cigarettes packages and further provides that the affixing stamps does not authorize actions that are otherwise prohibited
- provides that the penalties for the first offense shall be suspension; subsequent violations would result in revocation of the wholesaler's permit.
- allows the holder of an interim permit to possess cigarettes not affixed with stamps for a period of 30 days after the expiration of such permit.
- provides that an interim permit that will be valid until March 1, 2000, may be issued to a permit holder who has continuously held a permit since July 1, 1997 through March 1, 1999, without a manufacturer's affirmation form.
- provides that the department may revoke the registration of a primary source of supply or impose civil penalties for violation of s. 210.155(2).
- provides civil penalty caps for violations of 210.155.

VII. SIGNATURES:

COMMITTEE ON GOVERNMENTAL RULES AND REGULATIONS:

Prepared by:

Staff Director:

Veronica P. Alvarez

David M. Greenbaum

AS REVISED BY THE COMMITTEE ON FINANCE AND TAXATION:

Prepared by:

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George T. Levesque

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