

[Assembly Bill 2770](#) (Nazarian)

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Program: Cigarette & Tobacco Products Licensing Act (Licensing Act)

Sponsor: Author

Business and Professions Code (BPC) Sections 22973 and 22977.1

Effective January 1, 2017

Summary: This bill:

- Revises the due date for the BOE's report to the Legislature regarding the funding adequacy of the Licensing Act, and
- Requires the report to include information on the State Auditor's recommendation to eliminate the excess fund balance in the Cigarette and Tobacco Products Compliance Fund (Compliance Fund).

Summary of Amendments: Since the previous analysis, the bill was amended to revise the due date of the funding adequacy report, from January 1, 2020 to July 1, 2018.

Purpose: To provide additional funding for cigarette and tobacco products tax compliance enforcement.

Fiscal Impact Summary: None.

Existing Law: Cigarette and Tobacco Products Licensing Act of 2003.¹ The Licensing Act requires the BOE to administer a statewide program to license cigarette and tobacco products manufacturers, importers, distributors, wholesalers, and retailers. BPC Section 22972 requires a retailer to have a license to sell cigarettes and tobacco products in this state. Section 22972 further requires a retailer to obtain a separate license for each retail location that sells cigarettes and tobacco products. Similar license requirements are imposed on distributors and wholesalers under Section 22977.

BPC Section 22973 requires a one-time \$100 license fee to be paid with each retailer license application. Effective June 9, 2016, the retailer license fee increases to \$265. A retailer must obtain a separate license for each retail location, but may submit one application for those licenses. A retailer must annually renew their license, but until December 31, 2016, no fee is charged. Operative January 1, 2017, a \$265 per retail location renewal fee will be imposed.

BPC Section 22977.1 requires distributors and wholesalers to pay a \$1,000 fee with each license application or renewal application submitted, as required under Section 22977. A license is also required for each location. Operative January 1, 2017, the distributor and wholesaler license fee increases to \$1,200 per location.

BPC Sections 22973 and 22977.1 requires the BOE to report back to the Legislature, no later than January 1, 2019, regarding the adequacy of funding for the Licensing Act. The report shall include data and recommendations about whether the annual licensing fee funding levels are set at an appropriate level to maintain an effective enforcement program.

Cigarette and Tobacco Products Tax Law² (CTPTL). Existing law imposes an 87-cent per package of 20 (43 ½ mills per cigarette) cigarette tax. The CTPTL requires tax payment through the use of stamps or meter impressions that a distributor affixes on each cigarette package prior to the distribution.

RTC Section 30123 imposes a tax upon the distribution of tobacco products, based on the wholesale cost of these products at a tax rate that is equivalent to the combined rate of tax imposed on cigarettes. In addition, Section 30131.2 imposes an additional tobacco products tax at a rate equivalent to the \$0.50 per pack cigarette tax. The BOE annually determines the tobacco products tax rate based on the March

¹ Division 8.6 (commencing with Section 22970) of the BPC.

² Part 13 (commencing with Section 30001) of Division 2 of the Revenue and Taxation Code (RTC).

This staff analysis is provided to address various administrative, cost, revenue and policy issues; it is not to be construed to reflect or suggest the BOE's formal position.

1 wholesale cost of cigarettes. The tobacco products rate is 27.30% for fiscal year 2016-17. Distributors pay the tobacco products tax through the use of a tax return that reports the wholesale cost of the tobacco products distributed and calculates the tax due.

Proposed Law: This bill amends BPC Section 22973 to require the BOE, no later than July 1, 2018, to submit a report to the Legislature regarding the adequacy of funding for the Licensing Act. The report shall contain data and recommendations about whether the annual retailer, distributor, and wholesaler licensing fees are set at an adequate level to maintain an effective enforcement program. Additionally, the report shall include information on the BOE compliance with the recommendation in the [State Auditor's March 2016 report](#) to eliminate the excess fund balance in the Compliance Fund.

Background: In 2003, Assembly Bill (AB) 71 (J. Horton, Ch. 890) enacted the Licensing Act, which established a statewide licensure program administered by the BOE to help stem the tide of untaxed distributions and illegal sales of cigarettes and tobacco products. Currently, the BOE licenses approximately 37,000 retailers and 921 distributors and wholesalers to engage in the sale of cigarettes and tobacco products in California.

As AB 71 was developed and made its way through the Legislature, it was determined that the licensure fees would not permanently sustain the Licensing Act program. Since the Licensing Act enforces the CTPTL and directly benefits the funds established pursuant to that program, the funding for the Licensing Act would eventually shift to the cigarette and tobacco products tax funds: General Fund, Breast Cancer Fund, Cigarette and Tobacco Products Surtax Fund (Prop. 99) and California Children and Families Trust Fund (Prop. 10). However, there was concern about the Licensing Act program and the impact it would have on the cigarette and tobacco products tax funds if the Licensing Act expenses were more than the revenues generated. To address this concern, a sunset date of January 1, 2010, was incorporated into the Licensing Act to make sure the Licensing Act would not harm the cigarette and tobacco products tax funds. Furthermore, AB 71 included uncodified language to clarify that all revenues and expenses generated by the Licensing Act are to be allocated in the same manner as those revenues and expenses are allocated under the Cigarette and Tobacco Products Tax Law to make sure no one cigarette and tobacco product fund benefited or was burdened when the funding shift took place. In 2006, Assembly Bill 1749 (J. Horton, Ch. 501) repealed the sunset date for the Licensing Act due to the amount of additional excise tax revenues generated. The BOE has estimated that the Licensing Act and enhanced cigarette tax stamp generates an additional \$66.8 million in cigarette excise tax annually. The Licensing Act generates an additional \$24.5 million in additional tobacco products tax. The resulting additional sales and use tax revenue is estimated to be \$44.4 million annually.³

This year [ABx2 11](#) (Ch. 6, Stats. 2016, Nazarian) revised the Licensing Act to change a retailer's license fee from a one-time \$100 fee to an annual \$265 fee and increased the distributor/wholesaler license fee from \$1,000 to \$1,200, operative January 1, 2017. For new retail licenses, the license fee increase becomes effective June 9, 2016. That bill also requires the BOE to report back to the Legislature no later than January 1, 2019, regarding the adequacy of funding for the Licensing Act.

In General: The State Auditor's March 2016 report states that although it is legally permissible to use cigarette and tobacco products revenues to fund the Licensing Act, options exist to make the program self-supporting. The options include, among other things, retailer, wholesaler, and distributor license fee changes and increases, which the report includes as a recommendation. ABx2 11 increased the retailer, wholesaler, and distributor license fees.

The state audit also found that the Compliance Fund accumulated more than \$9 million in license fee revenues even though the License Act has a continuing funding shortfall. The report notes that these funds could be used to offset the Licensing Act costs and reduce the Compliance Fund shortfall. The audit report recommends that "unless the Legislature directs the board to eliminate the compliance fund's excess fund balance within a time frame of more than a year, the board should eliminated the

³ <http://www.boe.ca.gov/legdiv/pdf/CigaretteEvasion.pdf>.

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excess fund balance by June 30, 2017 by using it to offset the licensing program's annual funding shortfall."

Commentary:

1. **The May 12, 2016 amendments** revise the date by which the BOE must report to the Legislature the funding adequacy for the Licensing Act, from January 1, 2020 to July 1, 2018. The amendments also require the report to include information on the BOE's compliance with the State Auditor's recommendation to eliminate the excess fund balance in the Compliance Fund.
2. **Provisions not problematic.** The bill requires the BOE to include in the report to the Legislature regarding the Licensing Act funding information on the BOE's compliance with State Auditor's recommendation to eliminate the excess fund balance in the Compliance Fund. This provision does not materially affect the BOE.
3. **The ABx2 11 license fee provisions were already contained in this bill.** Previous staff analyses of this bill noted a revenue increase due to proposed retailer, wholesaler, and distributor license fee increases. These fee increases were contained in ABx2 11, which was signed into law May 4, 2016.

Costs: The bill results in insignificant administrative costs.

Revenue Impact: None.