

[Assembly Bill 2770](#) (Nazarian)

Date: Introduced

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

Sponsor: Author

Business and Professions Code (BPC) Sections 22973 and 22977.1

Effective January 1, 2017

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**Summary:** Revises the Licensing Act to change a retailer's license fee from a \$100 one-time fee to a \$265 annual fee and increases the distributor/wholesaler license fee from \$1,000 to \$1,200.

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

**Fiscal Impact Summary:** Estimated annual revenues of \$12 million.

**Existing Law: Cigarette and Tobacco Products Licensing Act of 2003.**<sup>1</sup> 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. A retailer must obtain a separate license (and pay \$100) for each retail location, but may submit one application for those licenses. A retailer must annually renew their license, but no fee is charged.

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.

**Cigarette and Tobacco Products Tax Law**<sup>2</sup> (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 wholesale cost of cigarettes. The tobacco products rate is 28.13% for fiscal year 2015-16. 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 increase the per-location retailer license application fee from \$100 to \$265. In addition, a retailer must remit an annual \$265 per-location license fee with each renewal application.

The distributor and wholesaler tobacco license fee increases from \$1,000 to \$1,200.

No later than January 1, 2020, the BOE shall 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.

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<sup>1</sup> Division 8.6 (commencing with Section 22970) of the BPC.

<sup>2</sup> 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.

**Background:** In 2003, Assembly Bill 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.<sup>3</sup>

### Commentary:

1. **Administrative start-up cost funding is essential.** The bill increases the fee and requires annual retailer license renewal on and after January 1, 2017. As a result, the BOE must begin to implement the bill in fiscal year 2016-17. However, the BOE's 2016-17 budget does not include funding to implement the bill. Consequently, the BOE requires an adequate appropriation to cover administrative implementation costs.
2. **Effect on the Compliance Fund.** Currently, the BOE's Licensing Act enforcement costs exceed licensing fee revenues. The Licensing Act authorizes the various cigarette and tobacco products tax funds<sup>4</sup> to make up the difference.

This bill relieves funding pressure by both increasing fees and requiring annual retailer license renewal. See Revenue Estimate for estimated additional revenue explanation.

3. **Related legislation.** [ABx2 11](#) (Nazarian) and [SBx2 10](#) (Beall) propose identical license fee increases. Other related bills include [SBx2 5](#) (Leno, et al) and [ABx2 6](#) (Cooper), which require the BOE to suspend or revoke a retailer's Licensing Act license and impose a civil penalty for furnishing a "tobacco product," including electronic cigarettes, to a minor. In addition, BOE must determine a one-time license fee for electronic cigarette retailers who are not subject to tax pursuant to the CTPTL. Since both this bill and the electronic cigarette retailer license fee bills (SBx2 5 and ABx2 6) amend Section 22973, BOE staff suggests double-jointing language to prevent chaptering out issues.

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

<sup>4</sup> Comprised of payments made to the state for the excise taxes on the distribution of cigarettes and tobacco products.

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**Administrative Costs:** The bill results in additional BOE administrative costs to notify retailers, rewrite computer programs, revise applications and publications, and answer inquiries from licensees. A detailed cost estimate is pending. As a point of reference, BOE staff estimated administrative costs for SBx2 10 and ABx2 11 to be \$18,000 for fiscal year 2015-16.

### Revenue Impact:

**Background, Methodology, and Assumptions.** BOE records indicate that 37,001 retailers were registered to sell cigarettes and tobacco products in fiscal year 2013-14.<sup>5</sup> There were 921 distributors and wholesalers registered. Licenses are valid for a 12-month period. About \$1.8 million in fees were remitted in fiscal year 2013-14.

Staff made the following assumptions:

- Staff assumes a uniform distribution of license renewals throughout the months of the year.
- No long-term growth is expected in the total number of registrants. This assumption is consistent with BOE records since the licensing program began in 2004. For example, in fiscal year 2005-06 there were 38,084 retailers selling cigarettes or tobacco products, slightly more registrants than today.
- Staff took into account that CVS Pharmacies will not sell tobacco related products and that San Francisco currently bans tobacco and e-cigarette sales in pharmacies.
- Changes in ownership of cigarette and tobacco products retailers as defined by this bill will be about 20% per year, the same as under current law. This implies annual fees of about 20% of the number of registrants even if there is no increase in the total number of registrants.

**Revenue Summary.** Based on these data and assumptions, the bill increases revenues by about \$12 million per year. Details are as follows:

<b>Estimated Revenue (Millions of Dollars)</b>	
Retailers	\$9.8
Retailer Turnover (20 Percent)	2.0
Wholesalers and Distributors	0.2
<b>Total</b>	<b>\$12.0</b>

This revenue estimate does not account for any further changes in economic activity that may or may not result from enactment of the proposed law.

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<sup>5</sup> *Taxes and Fees Administered by the California State Board of Equalization, FY 2013-14*, Publication 41, December 2014.

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