



**STATE BOARD OF EQUALIZATION
STAFF LEGISLATIVE BILL ANALYSIS**

DRAFT

Date Introduced:	02/27/09	Bill No:	SB 603
Tax:	Cigarette and Tobacco Products Licensing Act	Author:	Padilla
Related Bills:	SB 601 (Padilla) SB 602 (Padilla)		

BILL SUMMARY

This bill would make the following changes to the Cigarette and Tobacco Products Licensing Act of 2003¹ (Licensing Act):

- Require a retailer to pay annually the one-hundred dollar license fee to engage in the sale of cigarettes and tobacco products; and
- Limits the total number of retailer licenses issued in a county, and provides for the transfer of a license under specified conditions.

ANALYSIS

<p>Annual License Fee <i>Business and Professions Code Section 22973</i></p>

CURRENT LAW

Chapter 2, License for **Retailers** of Cigarettes and Tobacco Products, of the Licensing Act (commencing with Section 22972) provides that a retailer who sells cigarette and tobacco products in this state is required to have in place a license to engage in the sale of cigarettes and tobacco products and conspicuously display the license at each retail location in a manner visible to the public. A retail license is not assignable or transferable and can not be sold between businesses. A person who obtains a retailer license and stops doing business, or never starts doing business, or whose license is suspended or revoked, is required to immediately surrender the license to the Board.

A retailer that owns or controls more than one retail location where cigarette and tobacco products are sold is required to obtain a separate license for each retail location. Each retailer is required to submit a one-time license fee of one hundred dollars (\$100) with each application and may submit a single application for those licenses with a license fee of one hundred dollars (\$100) per location. A "retail location" is defined to mean any building from which cigarettes or tobacco products are sold at retail or a vending machine.

Additionally, Section 22973 authorizes the Board to investigate the truthfulness and completeness of the information provided in a retailer's application. The Board may also issue a license without further investigation to an applicant for a retail location if that applicant holds a valid license from the Department of Alcoholic Beverage Control (ABC) for that same location. A license is valid for a 12-month period, and is renewed annually. If a license is reinstated after its expiration, the retailer, as a condition

¹ Division 8.6 (commencing with Section 22970) of the Business and Professions Code.

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precedent to its reinstatement, is required to pay a reinstatement of one hundred dollars (\$100).

Section 22973.1 provides that the Board is required to issue a license to a retailer upon receipt of a completed application and payment of the fees, unless otherwise specified. Any person or retailer convicted of a felony under the Cigarette and Tobacco Products Tax Law would not be issued a license, or if that person holds a license, that license would be revoked. Any retailer who is denied a license may petition for a redetermination of the Board's denial within 30 days after service upon that retailer of the notice of the denial.

Chapter 3, License for **Wholesalers and Distributors** of Cigarettes and Tobacco Products, of the Licensing Act (commencing with Section 22975) requires that every distributor and wholesaler must annually obtain and maintain a license to engage in the sale of cigarettes or tobacco products. Every distributor and wholesaler must file an initial application and a renewal application accompanied by a fee of \$1,000 for each location. The fee is for a calendar year and may not be prorated. In addition, Chapter 4, License and Administration Fee for **Manufacturers and Importers**, of the Licensing Act (commencing with Section 22979) requires every manufacturer and importer to maintain a license to engage in the sale of cigarettes or tobacco products and to pay a one-time fee.

As provided in Sections 22990 and 22991 all moneys collected pursuant to of the Licensing Act are deposited in the Cigarette and Tobacco Products Compliance Fund (Compliance Fund) and are available for expenditure, upon appropriation by the Legislature, solely for the purpose of implementing, enforcing, and administering the Licensing Act.

PROPOSED LAW

This bill would amend Section 22973 to impose an annual \$100 per location license fee upon a retailer to engage in the sale of cigarettes or tobacco products.

This provision would be operative January 1, 2010.

BACKGROUND

In 2003, Assembly Bill 71 (J. Horton, Ch. 890) enacted the Licensing Act, which established a statewide licensure program administered by the Board to help stem the tide of untaxed distributions and illegal sales of cigarettes and tobacco products. Currently, the Board has approximately 38,000 retailers and 1,000 distributors and wholesalers licensed 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 Cigarette and Tobacco Products Tax Law 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

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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 Board has estimated that the Licensing Act and enhanced cigarette tax stamp generates an additional \$87.7 million in cigarette excise tax annually. The Licensing Act generates an additional \$17.5 million in additional tobacco products excise tax. The resulting additional sales and use tax revenue is estimated to be \$49.2 million annually. The breakdown by fund² is as follows:

Cigarettes		
Distributions (Millions of Packs)	n.a	100.8
Excise Taxes	\$0.87	\$87.7
General Fund	\$0.10	\$10.1
Breast Cancer	\$0.02	\$2.0
Proposition 99	\$0.25	\$25.2
Proposition 10	\$0.50	\$50.4
Sales and Use Taxes		
Average Retail Price Per Pack	\$4.91	
Retail Value of Cigarette Sales	n.a	\$495.0
Sales and Use Taxes, Total	9.00%	\$44.5
State General Fund	6.00%	\$29.7
Fiscal Recovery Fund (0.25%)	0.25%	\$1.2
Local	2.00%	\$9.9
Transit	0.75%	\$3.7
Tobacco Products		
Wholesale Sales	n.a.	\$38.8
Excise Taxes	45.13%	\$17.5
Proposition 99	28.66%	\$11.1
Proposition 10	16.47%	\$6.4
Sales and Use Taxes		
Retail Mark-Up Over Wholesale Price	35%	n.a.
Estimated Value of Retail Sales	n.a.	\$52.4
Sales and Use Taxes, Total	9.00%	\$4.7
State General Fund	6.00%	\$3.1
Fiscal Recovery Fund (0.25%)	0.25%	\$0.1
Local	2.00%	\$1.0
Transit	0.75%	\$0.4
Total Excise and Sales and Use Taxes		\$154.5
Totals may not sum due to rounding.		

² Assumptions: Cigarette revenues would have declined 3% per year without licensing or the new stamp. Tobacco products sales and revenues would not have changed without licensing. Thirty-month implementation period for both licensing and the new stamp (January 1, 2004 through June 30, 2006). Revenues are annual and ongoing. Tobacco products tax rate is for fiscal year 2007-08.

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COMMENTS

1. **Sponsor and purpose.** This bill is sponsored by the author. The proposed annual tobacco retailer license renewal fee is intended to fund enforcement and compliance laws.
2. **How is the Board currently funded under the Licensing Act?** The Board's costs to enforce and administer the Licensing Act are funded with revenues deposited into the Compliance Fund, which includes license fee revenues, penalties and fines. The Compliance Fund fully reimbursed those costs through fiscal year 2005-06. In 2006-07, the Board's administrative costs were partially offset with cigarette and tobacco products tax revenues. As of 2007-08, substantially all of the Board's costs will be funded in this manner in order to cover the difference between Compliance Fund revenues and expenses. Below is a funding summary for the Licensing Act program, as reflected in the 2009-10 Governor's Budget:

Fund	2007-08	2008-09	2009-10
General Fund	\$928,000	\$1,047,000	\$1,261,000
Breast Cancer Fund	186,000	209,000	251,000
Cigarette and Tobacco Products Surtax Fund	2,319,000	2,618,000	3,135,000
CA Children and Families First Trust Fund	4,641,000	5,236,000	6,273,000
Cigarette and Tobacco Products Compliance Fund	1,198,000	1,130,000	682,000
Total	\$9,272,000	\$10,240,000	\$11,602,000

3. **The fees generated by this measure would not fully offset the shortfall in the Compliance Fund.** The Board estimates this bill would generate approximately \$3,820,000 in additional revenue that would be deposited into the Compliance Fund (see the Revenue Estimate below). Since the annual shortfall amount appears to be approximately \$8 million beginning in fiscal year 2007-08, this bill would not fully eliminate the Compliance Fund shortfall.
4. **While the local city and county licensing laws generally require an annual licensing fee, the state's Licensing Act currently imposes only a one-time retailer license fee.** Many local cities and counties in California have adopted local tobacco retailer licensing laws, which require a retailer to pay an annual licensing fee and to be subject to suspension or revocation of that license if they are found selling tobacco to minors. Therefore, California retailers engaged in the sale of cigarettes or tobacco products and located in a city or county that has adopted local tobacco retailer licensing laws have two licenses (state and city/county). For example, in addition to the one-time \$100 state tobacco retail license fee, the City of Santa Ana, located in Orange County, requires a \$635 annual city tobacco retail license fee,³

³ City of Santa Ana, Tobacco Retail License Ordinance: [Tobacco Retail License](#)

while the County of Los Angeles charges a \$235 annual fee for a county tobacco retail license.⁴

5. **Retailer renewal fee – suggested amendments.** This bill would require a retailer to pay a license renewal fee and also require the license fee to be submitted annually thereafter per location. In addition, the bill strikes the language that allows a retailer to submit a single application for all retail locations. The purpose of this provision is to simplify the application and renewal process for retailers and reduce the number of applications received and processed by the Board. However, Board staff prefers that the bill be amended to add back this provision.

Further, the provisions could be construed to mean that a retailer that allows their license to expire must only pay the reinstatement fee to have the license reinstated. It is suggested that the author amend the bill to clarify that the renewal fee must accompany the renewal application, and that the reinstatement fee is in addition to the annual retailer license fee. Board staff is available to work with the author's office on suggested language.

6. **Would all licenses held by a retailer be renewed at the same time?** It depends on the start date for each of the retailer's locations. Under existing law, a retailer license is valid for a 12-month period and must be renewed annually. Accordingly, retailers are required to annually renew their license on or before the first day of the month of the retail location start date. For example, if a retailer is licensed to engage in the sale of cigarette or tobacco products on May 17th, they would be required to renew their license on or before May 1st of the following year.

Many retailers also engage in the sale of cigarette or tobacco products from more than one retail location. These additional locations (sub-locations) may have a different start date than the original (master) retail location. Since the Licensing Act does not provide a specific renewal date for a retail license, the Board aligns all of the retailer's sub-location licenses with the renewal date for their master license. The purpose of aligning the renewal dates is to relieve retailers that have multiple locations and various start dates from the burden of renewing each individual license at different dates throughout the year. Although the sub-location licenses may have been valid for less than 12 months, the retailer is not adversely affected by the shortened initial year for which the \$100 licensing fee was paid since the retailer license fee is a one-time fee.

This bill proposes an annual \$100 retailer license fee, which could result in a retailer not wanting their sub-location licenses aligned to the master license since they may not receive a full 12 month license for the sub-location license fee in the initial year. In addition to the Board's increased workload in processing multiple applications for each retail location each year, the multiple renewal dates and applications could result in a retailer allowing a license to accidentally expire. An expired license is subject to reinstatement fees, which would be in addition to the proposed renewal fee, and subjects the retailer to citations for unlicensed sales of such products, which for the first offense results in the issuance of a "Warning Notice" to the licensee, and for failure to display a license which carries a five hundred dollar (\$500) fine.

It is suggested the bill be amended to make all cigarette and tobacco products retailer licenses held by a retailer valid for the same period thereby aligning sub-

⁴ County of Los Angeles, Tobacco Retail License:
http://www.lapublichealth.org/tob/pdf/Retailer%20FAQ%20v.6_FINAL.pdf

location licenses with the retailer's master account. This provision would make it more convenient for retailers to renew by using one renewal application rather than a separate renewal application for each location. It would also make the renewal process more efficient for retailers by eliminating multiple renewal dates throughout the year, which could lead to a retailer allowing their license to expire and subjecting that retailer to reinstatement fees and related penalties. The provision would also significantly reduce administrative costs to the Board for computer programming, license processing, following up on closed-out retailer licenses, and reinstating closed-out licenses. The Board is willing to work with the author to draft appropriate amendments.

- 7. Related legislation.** SB 601 (Padilla) adds provisions to the Licensing Act to prohibit the issuance of a retail license for a location within 1,000 feet of a school, and limits retail licenses to “traditional retail locations.”

SB 602 (Padilla) adds provisions to the Licensing Act to prohibit the issuance of a new license to a retailer in an “area of overconcentration,” and makes reporting requirement changes related to sales to minors.

Retailer License Limit per County

Business and Professions Code Section 22973.3

CURRENT LAW

As previously explained, Business and Professions Code Section 22972 requires a retailer who sells cigarette and tobacco products in this state to have in place a license to engage in the sale of cigarettes and tobacco products and conspicuously display the license at each retail location in a manner visible to the public, and is required to obtain a separate license for each retail location. A retailer that owns or controls more than one retail location where cigarette and tobacco products are sold is required to obtain a separate license for each retail location. Each retailer is required to submit a one-time license fee of one hundred dollars (\$100) with each application and may submit a single application for those licenses with a license fee of one hundred dollars (\$100) per location. A "retail location" is defined to mean any building from which cigarettes or tobacco products are sold at retail or a vending machine.

Additionally, Section 22973 authorizes the Board to investigate the truthfulness and completeness of the information provided in a retailer's application. The Board may also issue a license without further investigation to an applicant for a retail location if that applicant holds a valid license from the Department of Alcoholic Beverage Control (ABC) for that same location. A license is valid for a 12-month period, and is renewed annually.

Section 22973.1 provides that the Board is required to issue a license to a retailer upon receipt of a completed application and payment of the fees, unless otherwise specified. Any person or retailer convicted of a felony under the Cigarette and Tobacco Products Tax Law would not be issued a license, or if that person holds a license, that license would be revoked. Any retailer who is denied a license may petition for a redetermination of the Board's denial within 30 days after service upon that retailer of the notice of the denial.

PROPOSED LAW

This bill would add Section 22973.3 to the Licensing Act to limit the total number of cigarette and tobacco retailer licenses issued in a county to one for each 2,500 persons, or fraction thereof, over 18 years old in the county of the retail location. Applications for a retailer license will be granted in the order they are received, subject to the Licensing Act requirements.

In counties where the ratio of retail licenses exceed the specified ratio of one to each 2,500 adults, the Board would be prohibited from issuing additional retail licenses, except for a renewal or transfer. The transfer of a license would be allowed under either of the following circumstances:

- For the continued use at the same location upon the sale or transfer of the business holding the license, or
- For use at another location by the holder of the current license, upon certification by the department that the new location is not in an area of overconcentration.

This provision would be operative January 1, 2010.

COMMENTS

1. **Sponsor and purpose.** This bill is sponsored by the author and is intended to reduce the availability of tobacco products in California communities to prevent youth from tobacco use.
2. **Board's mission and tasks.** The mission of the Board is to serve the public through fair, effective, and efficient tax administration. The provisions in this bill may represent a departure from our traditional "tax collection" functions. In general, the Board requires a license, permit, or registration for the various tax and fee programs that we administer. Essentially, the purpose of the licensing/registration/permit is to ensure collection of vital revenues for the state.

According to the legislative findings in the Licensing Act, the licensing of manufacturers, importers, wholesalers, distributors, and retailers was a comprehensive program to reduce untaxed distribution and illegal sales of cigarette and other tobacco products in California. Although the Licensing Act provided stricter retailer licensing requirements, compared to permit requirements for sales and use tax, the stricter standards were established to support the overall goal of improving tax collection. The licensing restrictions that this bill proposes appear to be related to health, public safety, or other non-tax purposes. Is the Licensing Act the proper venue for the proposed changes?

3. **Placing a cap on the number of licenses in a county.** This bill effectively places a cap on the total number of licenses that may be issued in a county. The total number of licenses is limited to one license for each 2,500 persons at least 18 years old. In the case where a county has a ratio greater than 1 to 2,500, it appears that a moratorium is effectively put in a place. Besides the renewal or "transfer" provisions provided in the bill, would there be any other exceptions? A reinstatement of a license after a suspension is not considered a renewal, but would the Board be authorized to reinstate the license where a moratorium exists? The author may want to consider clarifying the effect of a reinstatement of a license.

Additionally, there are no provisions for the determination of population in the county. What population basis would the Board use to initially determine the population? How often would the Board adjust the county population? Does the Board make the population determination, or would the Department of Finance, or the federal census? The author should add provisions specifying important population details.

4. **What would the effect of a county cap be?** This bill provides that when the number of current licenses exceeds the county ratio, an existing license may be transferred under one of two conditions: (1) continued use at the same location when the business holding the license is sold or transferred; or, (2) use at another location by the holder of the license, as long as it is not in an area of overconcentration. Are these the only circumstances that a license can be transferred? Shouldn't there be separate provisions detailing the actions involved in the transfer of a license? Similar to Section 24049 of the ABC Act, should the Board be allowed to refuse transfer of a license if the license holder has an outstanding tax liability? Who would be able to sell or have a right to the proceeds? Wouldn't the Board be precluded from issuing a "new license" until the ratio in the county is reduced to the cap amount? Would that be the same as a moratorium? What would happen when a retailer in an county that exceeds the cap sells the business, won't the license have value?
5. **What effect would this provision have on the Cigarette and Tobacco Products Compliance Fund?** Currently, the Board's enforcement costs exceed the amount of revenues from the licensing fees with the shortfall made up by the various cigarette and tobacco tax funds (comprised of payments made to the state for the excise taxes on the distribution of cigarettes and tobacco products). If the number of retail licenses decreases and the Board has additional licensing investigation duties, then this may result in additional shortfalls in funding from the Compliance Fund.

As Assembly Bill 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 Cigarette and Tobacco Products Tax Law 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. AB 71 also 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. Since this measure is intended to address youth smoking and not the administration and collection of cigarette and tobacco products taxes, it is unclear how this measure would be funded. While the Licensing Act provides that all moneys in the Compliance Fund are to be used for the purpose of implementing, enforcing and administering the Licensing Act, this measure could result in a significantly larger shortfall in the Fund even with the proposed annual \$100 retailer license fee, thus shifting a larger burden of the expense to the cigarette and tobacco products tax funds. As such, it could be construed that the cigarette and tobacco products funds, which existing law requires

to be used for the administration and collection of the cigarette and tobacco products taxes⁵, are being used to fund enforcement of youth smoking.

8. **Local retailer licensing requirements and possible preemption issues.** Many local cities and counties in California have adopted local tobacco retailer licensing laws, which require a retailer to pay an annual licensing fee and be subject to suspension or revocation of that license if they are found selling tobacco to minors. Therefore, California retailers engaged in the sale of cigarettes or tobacco products and located in a city or county that has adopted local tobacco retailer licensing laws have two licenses (state and city/county). This also means that some retailers may have local licensing requirements and restrictions unrelated to payment of excise taxes. For example, Los Angeles county has a tobacco retail license program in which they indicate the necessity of having both a state and county license:

I already have a state tobacco license issued by the California Board of Equalization. Why do I need a tobacco license from the County?

The tobacco license issued by the California Board of Equalization is meant to curb tobacco tax fraud and the counterfeiting of tobacco products. That license does not preempt local jurisdiction from adopting local tobacco licenses. The Los Angeles County Board of Supervisors adopted this ordinance on December 18, 2007 to encourage responsible tobacco retailing and to discourage violations of federal, state and local tobacco-related laws, especially those that prohibit the sale or distribution of tobacco products to minors.

To legally sell tobacco products in the unincorporated areas of the County you will need a valid state tobacco license and a County tobacco license.

http://www.lapublichealth.org/tob/pdf/Retailer%20FAQ%20v.6_FINAL.pdf

Section 22971.3 provides that, with the exception of collection of state taxes, nothing in the Licensing Act preempts or supersedes local tobacco control laws. However, the proposed state licensing limitation appears to be related to health and public safety, rather than collection of state taxes. Would the proposed licensing limitations in a county preempt or supersede related local tobacco control laws? It may be necessary for the author to authorize the State to preempt or supersede local tobacco control laws in order to prevent conflicts between local and state licensing requirements.

9. **Related legislation.** SB 601 (Padilla) adds provisions to the Licensing Act to prohibit the issuance of a retail license for a location within 1,000 feet of a school, and limits retail licenses to “traditional retail locations.”

SB 602 (Padilla) adds provisions to the Licensing Act to prohibit the issuance of a new license to a retailer in an “area of overconcentration,” and makes reporting requirements changes related to sales to minors.

⁵ R&TC §§30124, 30125, 30131.3 and 30131.4.

COST ESTIMATE

Significant administrative costs would be incurred for both provisions in this bill. Costs would be related to notifying retailers, revising and/or developing computer programming, revising applications and publications, developing procedures to determine the number of licenses per county, developing regulations and procedures to identify and issue licenses to retailers in a county, providing for additional staff time to investigate applications and license transfers, developing procedures to handle transfers of licenses, address legal issues, and answering inquires from licensees. A detailed cost estimate is pending.

REVENUE ESTIMATE**BACKGROUND, METHODOLOGY, AND ASSUMPTIONS**

According to the Board's Excise Taxes Division, there are approximately 38,200 licensed retail locations selling cigarettes or tobacco products in California. This figure has been fairly stable since the inception of the Licensing Act. Accordingly, the proposed annual renewal fees would total approximately \$3,820,000 (\$100 x 38,200).

REVENUE SUMMARY

Retailer license fee revenues would increase by \$3,820,000 annually under this measure.

We are not able, however, to quantify the revenue impact for the retailer licensing cap provision in this bill. But it could result in a negative impact on excise taxes and licensing fees due to less convenience for consumers seeking to purchase cigarettes in some areas.

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