



LEGISLATIVE FISCAL OFFICE
Fiscal Note

Fiscal Note On: HB 537 HLS 13RS 1063
Bill Text Version: ORIGINAL
Opp. Chamb. Action:
Proposed Amd.: w/ PROP HSE COMM AMD
Sub. Bill For.:

Date: April 14, 2013 3:36 PM Author: JACKSON, K
Dept./Agy.: Revenue Analyst: Greg Albrecht
Subject: Tobacco Tax Increase

TAX/TOBACCO TAX OR +\$64,000,000 GF RV See Note Page 1 of 2
(Constitutional Amendment) Levies an additional tax on cigarettes and other tobacco products and authorizes the dedication of such monies
Current law imposes an excise tax on cigarettes of 36¢ per 20-pack. Tax rates on other tobacco products are: cigars at 8% - 20% of manufacturers invoice price, 33% for smoking tobacco, and 20% for smokeless tobacco.

Proposed law, with proposed House Committee amendments, increases the tax rates on tobacco products. On cigarettes the proposed tax increase is 32¢ per 20-pack (to a new tax rate of 68¢ per 20-pack), on all other tobacco products the proposed new tax rate is 68% of the manufacturers invoice price; an increase for cigars from the current rates of 8% to 20%, and on smoking tobacco and smokeless tobacco an increase from the current rates of 33% and 20%, respectively.

Effective January 1, 2014.

Table with 7 columns: EXPENDITURES/REVENUES, 2013-14, 2014-15, 2015-16, 2016-17, 2017-18, 5-YEAR TOTAL. Rows include State Gen. Fd., Agy. Self-Gen., Ded./Other, Federal Funds, Local Funds, and Annual Total for both categories.

EXPENDITURE EXPLANATION

In the past, the Department of Revenue has indicated that it will incur one-time costs to notify affected taxpayers of the tax rate increases, to revise tax forms, and make tax system programming changes. In addition, these relatively large tax rate increases may warrant enhancements of security features of tax stamps to deter counterfeiting, entailing a recurring cost increase for more expensive tax stamps. Rough estimates of these costs in the past have totaled \$150,000 initially, and \$75,000 per year thereafter. Initial costs are likely to be incurred in FY14.

REVENUE EXPLANATION

Tobacco taxes on cigarettes currently make up approximately 81% of total tobacco tax collections. The state cigarette tax was increased in 1990, 2000, and 2002, and the federal tax was increased in 2009. In each of those cases additional collections were less than the simple average yield of 1¢ of tax (prior to the tax rate increase) implied. In the last state episode (2002), the new collections level was only about 82% of what would be implied from the simple average yield, and only 55% with the last federal episode (2009). That is, total tax-paid sales decline when prices increase (in these cases from a tax increase) as consumers avoid the tax by purchasing the product in lower tax locales and reduce real consumption of the product altogether.

A simple calculation of revenue gain based on the current average yield of 1¢ of tax would result in an anticipated annual gain of some \$102 million in FY14 from the cigarette tax increase proposed in this bill. However, this assumes no purchase response on the part of consumers. A somewhat more complicated calculation encompassing average prices, state & local sales taxes, industry markups, and a cross-border or state-only purchaser response of -.98 results in an anticipated annual gain of some \$80 million in FY14. Adjusting the simple average yield calculation above for what has actually happened with past state tax increases compared to the simple average yield expectation at the time can result in a revenue gain of as little as \$68 million (actual gains have averaged 33% less than an average yield would suggest, but with considerable variation).

Previous state tax increases were individually relatively small (4¢, 4¢, and 12¢, respectively; percent increases of 25%, 20%, and 50%) compared to the 32¢ increase of this bill (nearly doubling the current tax), while the federal increase was relatively large at 61.66¢ (158%). Texas, Arkansas, and Mississippi all have higher current tax rates of \$1.41/pack, \$1.15/pack, and 68¢/pack, respectively. These tax rate differentials are likely to have generated sales and tax receipts in Louisiana from neighboring state residents. The tax rate increase proposed by this bill will work to reduce this effect with respect to Texas and Arkansas, possibly negate it with respect to Mississippi.

Additional internet sales may also reduce the revenue gain potential from the bill. Without much certainty as to the magnitude of these effects under this bill's tax increase, an average of the two calculations above that account for purchase response is utilized for the bill's cigarette tax increase : \$74 million per full year, adjusted to \$37 million in the second half of FY14, given an effective date of 1/1/2014.

Additional revenue receipts from other tobacco products are estimated at \$27 million for the second half of FY14, doubling to \$55 million in FY15 and beyond (discussed on page 2).

- Senate Dual Referral Rules House
13.5.1 >= \$100,000 Annual Fiscal Cost {S&H} 6.8(F) >= \$500,000 Annual Fiscal Cost {S}
13.5.2 >= \$500,000 Annual Tax or Fee Change {S&H} 6.8(G) >= \$500,000 Tax or Fee Increase or a Net Fee Decrease {S}

Signature of John D. Carpenter
John D. Carpenter
Legislative Fiscal Officer

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CONTINUED EXPLANATION from page one:

The 19% balance of current total tobacco tax collections comes from sales of "low" invoice price cigars (no more than \$120/1000 cigars) and "high" invoice price cigars (more than \$120/1000), smoking tobacco, and smokeless tobacco. This bill increases the tax rates on all of these products to a new total rate of 68% of manufacturers invoice price (from 8% on "low" cigars, from 20% on "high" cigars, from 33% on smoking tobacco, and from 20% on smokeless tobacco). There is no recent Louisiana tax change history with respect to these particular products from which to directly assess an estimate of tax-paid purchase response. This proposed tax rate ranges from 2 times to 8.5 times the current tax rates for these products. A simple average yield calculation for these products results in a revenue gain of \$76 million. Applying the same discount from average yield implied in the cigarette average gain above (27%) results in a full year estimate of revenue gain of \$55 million in FY14, adjusted to \$27 million in the second half of FY14, given an effective date of 1/1/2014.

Tax rate changes that do not apply to current inventories can elicit wholesaler stockpiling and work-off behavior that distorts monthly collections pattern, requiring adjustment to estimates for particular fiscal years (stockpiling late in the current fiscal year, worked off early in the subsequent fiscal year). The effective date of this bill (midway through FY14) makes stockpiling and work-off adjustments unnecessary from the fiscal year's perspective since that wholesaler behavior will likely occur entirely within a single fiscal year.

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| <u>Senate</u> | <u>Dual Referral Rules</u> | <u>House</u> |
| <input type="checkbox"/> 13.5.1 >= \$100,000 Annual Fiscal Cost {S&H} | | <input type="checkbox"/> 6.8(F) >= \$500,000 Annual Fiscal Cost {S} |
| <input checked="" type="checkbox"/> 13.5.2 >= \$500,000 Annual Tax or Fee Change {S&H} | | <input type="checkbox"/> 6.8(G) >= \$500,000 Tax or Fee Increase or a Net Fee Decrease {S} |

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