

SENATE STAFF ANALYSIS AND ECONOMIC IMPACT STATEMENT

(This document is based on the provisions contained in the legislation as of the latest date listed below.)

Prepared By: Regulated Industries Committee

BILL: SPB 7042

SPONSOR: For consideration by Regulated Industries Committee

SUBJECT: Cigarette Taxes

DATE: February 2, 2005

REVISED: _____

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	<u>Oxamendi</u>	<u>Imhof</u>	_____	Pre-meeting
2.	_____	_____	_____	_____
3.	_____	_____	_____	_____
4.	_____	_____	_____	_____
5.	_____	_____	_____	_____
6.	_____	_____	_____	_____

I. Summary:

The bill amends s. 210.021, F.S. to require that a dealer or agent must remit the cigarette taxes imposed by ch. 210, F.S, by electronic funds transfer during the dealer or agent's initial period of licensure or appointment, but not to exceed 12 months. The bill authorizes the Division of Alcoholic Beverages and Tobacco (DABT or division) in the Department of Business and Professional Regulation (DBPR) to adopt rules to administer this provision.

The bill amends s. 210.08, F.S., to increase from \$10,000 to \$20,000 the maximum amount for the surety bond, certificate of deposit, or revocable letter of credit that must be filed with the DABT for payment of taxes.

The bill amends s. 210.18, F.S., to require state law enforcement officers, in addition to the sheriffs, deputy sheriffs, and police officers, to report the seizure of unstamped cigarettes to the DABT. It requires that the division maintain records of the number of seizures and number of seized cigarettes.

This bill substantially amends the following sections of the Florida Statutes: 210.021, 210.08, and 210.18.

II. Present Situation:

Cigarette Excise Tax

The division oversees the collection of excise taxes from the sale of cigarettes and other tobacco products. Section 210.15, F.S., requires that every person, firm or corporation desiring to deal in cigarettes in Florida as a distributing agent, wholesale dealer, or exporter must apply for a

cigarette permit. The current excise tax in Florida ranges from 16.9 cents per package to 67.8 cents per package, depending on the number of cigarettes per package.¹ The current excise tax is 33.9 cents per standard 20-cigarette pack.²

Section 210.06, F.S., requires that every stamping agent affix a tax stamp as evidence that the excise tax has been paid before the cigarettes can be offered for sale in this state. Sections 210.02 and 210.04, F.S., provide that excise taxes must be paid by the wholesale dealer upon the first sale or transaction inside the state whether or not such sale or transfer is to the ultimate purchaser or consumer. Because wholesaler dealers may purchase cigarettes from other wholesaler dealers, only the first sale is taxed. Distributing agents, acting as agents of the manufacturers, are not required to pay taxes for the distribution of cigarettes to wholesale dealers.

Collected excise taxes are paid to the division. Stamps representing various denominations of tax are purchased in bulk by the stamping agents and are affixed to packages as proof of payment. Cigarettes that are not properly stamped may not be sold in Florida. The amount of the tax then becomes a part of the price of the cigarettes to be paid by the purchaser or consumer. According to the division, it collected \$416 million in cigarette excise taxes from stamping distributors for the Fiscal Year 2003-04.

Contraband Cigarettes

A recent U.S. Government Accountability Office (GAO) report found a link between international terrorist groups and the illicit trafficking in contraband cigarettes and counterfeit cigarette tax stamps.³ According to the GAO report, law enforcement officials have determined that international terrorist groups use cigarette trafficking to raise funds. The extent of the contraband cigarette problem is unknown principally because of the illegal nature of the conduct, however, federal seizures of contraband cigarettes have increased dramatically in recent years from 12 seizures in 1998 to 191 seizures in 2003.⁴

The scope of counterfeit or untaxed cigarette sales in Florida is also unknown. The Florida Department of Law Enforcement (FDLE) and the division do not maintain records of counterfeit cigarette seizures or related arrests. Section 210.18(7), F.S., requires sheriffs, deputy sheriffs, and police officers to report to the division the seizure of any unstamped cigarettes in order that the state may be kept informed as to the size and magnitude of the illicit cigarette business. According to the DBPR, the department is not aware of any local enforcement cigarette seizures without DABT agents in attendance. The department asserts that its district offices maintain contact with the local law enforcement officials and work in unison in any activities involving either alcoholic beverages or tobacco products. Accordingly, no reports of any seizures without DABT involvement have been reported to the division pursuant to s. 210.18(7), F.S. The division has not kept records of seizures.

¹ See ss. 210.02(3) and (4), F.S.

² Section 210.02(3)(b), F.S.

³ *Terrorist Financing: U.S. Agencies Should Systematically Access Terrorists' Use of Alternative Financing Mechanisms*, U.S. General Accounting Office, GAO-04-163, November 2003.

⁴ *Cigarette Smuggling: Federal Law Enforcement Efforts and Seizure Increasing*, U.S. General Accounting Office GAO-04-641, May 2004.

In addition to local law enforcement and the DABT, Department of Transportation (DOT) highway inspectors are a potential source of information regarding cigarette seizures. To date the DOT has had no contraband cigarette seizures because its motor carrier compliance officers, who are certified law enforcement officers, were not trained in the identification of contraband and unstamped cigarettes. However, in October 2004, the DOT began to train its officers regarding counterfeit and unstamped cigarettes.

The division's enforcement staff perceives that this is a prevalent problem in the state. The division states that, through their work with the Federal government, several million packs of cigarettes have been seized in the past five years. The division advises that although the total amount of counterfeit cigarettes entering the state is unknown, it believes that the number is growing.

Bond Requirements

Persons must obtain a stamping agent permit in order to obtain cigarette tax stamps. When tax stamps are purchased, the division anticipates a tax report the next month, and actively pursues any permitted cigarette wholesale dealer who does not file a report. According to the division and industry representatives, there is a growing problem in Florida with persons who apply for a wholesale dealer license and avoid paying taxes. These persons evade the excise taxes by purchasing the tax stamps with bank drafts that are subsequently returned for insufficient funds. These licensees then close their business before reporting and paying the taxes to the division.

According to the division, many of these operations involve cigarette brands not commonly recognized that are either purchased from unlicensed entities through customs or from small manufacturers, who do not report to the state on a monthly basis. These cigarettes brands are commonly referred to as private brands and as fourth-tier cigarettes. Florida law does not require manufacturers or importers to report to the division information regarding cigarettes sold from out-of-state to stamping agents, but most report this information voluntarily. However, according to the division, many do not report.

Stamping agents may purchase cigarette tax stamps by check or credit. For example, a typical roll of tax stamps costs over \$10,000. If a payment is made by check, and there are insufficient funds to cover the amount of the check, the bad check may not be identified for several weeks or months. During this time the stamping agent could amass a high bill for unpaid taxes. A credit payment could ultimately not be paid or also made with a bad check. Therefore, the taxes may not be collected before the stamping agent goes out of business.

Stamping agents must obtain a surety bond to cover the taxes, but the required bond does not cover the cost of a typical purchase of tax stamps. Section 210.08, F.S., requires a \$10,000 bond as surety for payment of all taxes. Section 210.08, F.S., authorizes the division to accept a bond that is not less than \$1,000, and prohibits the division to require a bond greater than \$10,000. The \$10,000 bond limit and \$1,000 bond minimum have been in effect since 1945, when the excise tax on cigarettes was two cents.⁵ As noted above, the excise tax is currently 33.9 cents per 20-cigarette pack.

⁵ See ss. 2 and 6, ch 22645, L.O.F. (1945).

A stamping agent may purchase tax stamps in excess of \$10,000 but is only required to purchase a bond of \$10,000. According to the division, individual tax stamp purchases in excess of \$10,000 are common, and the typical roll of stamps costs more than \$10,000. Also, according to the division, since the year 2000, the division has received approximately 14 bad checks from 10 stamping agents. After collecting on the bonds, two of the checks remain partially unpaid for a total outstanding amount of \$30,724. This does not include staff time to collect the checks and on the bond.

Section 210.021, F.S., permits the division to require a wholesaler to pay the tax by electronic funds transfer (EFT) if the stamping agent has paid \$50,000 or more in taxes during the previous year. According to the division, requiring all stamping agents to pay by EFT may lessen the non-payment problem because payments made with insufficient funds are less common when made by EFT than with check payments. In the addition, the division believes that requiring all new stamping agents to pay by cashiers checks for the first year of operation would establish the stamping agent as a permanent business with a reduced risk of going out of business and disappearing with a large outstanding tax bill.

Interim Project 2005-157

The Senate President approved interim project no. 2005-157, which reviewed Florida's tobacco settlement and the effect of the nonsettling manufacturers on the state's settlement payments.⁶ The purpose of the project was to determine if legislative action is necessary to protect the state's tobacco settlement revenue from diminution or significant loss. In the course of the project, issues related to the cigarette distribution system were addressed, and resulted in the following relevant recommendations:

- The Legislature should amend s. 210.08, F.S., to increase the maximum bond requirement for stamping agents. The maximum bond amount should be sufficient to cover the actual amount of tax stamps purchased. The Legislature should also authorize the division to require all new stamping agents to pay for tax stamps with a certified cashier's check or by EFT for the first year of operation in order establish that the stamping agent is a permanent business. These measures would reduce the risk of tax stamps being purchased with checks for insufficient funds.
- The Legislature should require that the division maintain statistics regarding seizures of counterfeit and contraband cigarettes, and related arrests in order to accurately assess the extent of any law enforcement and tax collection problems.
- The Legislature should amend s. 210.18(7), F.S., to require the Department of Transportation to report to the division the seizure of any unstamped and contraband cigarettes.

⁶ See Committee on Regulated Industries, *Florida Tobacco Settlement and Nonsettling Manufacturers*, report no. 2005-157, November 2004.

III. Effect of Proposed Changes:

Section 1. The bill amends s. 210.021, F.S. to require that a dealer or agent must remit the cigarette taxes imposed by ch. 210, F.S, by EFT during the dealer or agent's initial period of licensure or appointment, but not to exceed 12 months. The bill authorizes the DABT to adopt rules to administer this provision.

Section 2. The bill amends s. 210.08, F.S., to increase from \$10,000 to \$20,000 the maximum amount for surety bond, certificate of deposit, or revocable letter of credit that must be filed with the DABT for payment of taxes.

Section 3. The bill amends s. 210.18, F.S., to require state law enforcement officers, in addition to the sheriffs, deputy sheriffs, and police officers, to report the seizure of unstamped cigarettes to the DABT. It requires that the division maintain records of the number of seizures and the number of seized cigarettes.

IV. Constitutional Issues:**A. Municipality/County Mandates Restrictions:**

None.

B. Public Records/Open Meetings Issues:

None.

C. Trust Funds Restrictions:

None.

V. Economic Impact and Fiscal Note:**A. Tax/Fee Issues:**

None.

B. Private Sector Impact:

Cigarette dealers, agents, and distributing agents would be subject to a higher maximum surety bond, certificate of deposit, or revocable letter of credit in the amount of \$20,000 as a surety for payment of cigarettes excise taxes.

C. Government Sector Impact:

None.

VI. Technical Deficiencies:

None.

VII. Related Issues:

None.

This Senate staff analysis does not reflect the intent or official position of the bill's sponsor or the Florida Senate.

VIII. Summary of Amendments:

None.

This Senate staff analysis does not reflect the intent or official position of the bill's sponsor or the Florida Senate.
